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China and the European Union: future directions

José María Beneyto
Xinning Song
Chun Ding
(Editors)



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China and the European Union: future directions

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CEU Ediciones

Julián Romea 18, 28003 Madrid

Teléfono: 91 514 05 73, Fax: 91 514 04 30

Correo electrónico: ceuediciones@ceu.es

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Introduction

Gracia Abad

Any analysis of the current state of international affairs would require devoting a great deal of its efforts to the examination of the People's Republic of China, its policies, its capabilities, its approaches, as well as its position regarding a wide range of issues. Not in vain, the People's Republic of China is a rising power whose attitudes and policies will have a direct impact on the future development of the international system and the international relations within.

Thus, the importance of the People's Republic of China status as a permanent member of the United Nations Security Council, the impressive growth of both its GDP and its Defence Budget over the last few years and its relatively good performance through the global financial and economic crisis are all factors that might recommend to pay attention to the evolution of this country.

Furthermore, the prominence of the People's Republic of China might not be accidental. On the contrary, it might be considered as a consequence of a deliberate Chinese strategy in line with the so called "Peaceful Rise" (a concept later replaced by the terms "peaceful development" and "harmonious development", at least in some circles close to the Chinese high officials). The new terminology was meant to ease the latent fears arising from the so called "China threat", a concern closely connected with the Chinese rise itself. Ultimately, these new concepts might be considered, at least to some degree, as a reaction to the continuous demands on China to ensure its responsive behaviour.

Moreover, the Chinese strategy might be in accordance with the diplomatic activism displayed by the People's Republic of China in many geographical areas and involving very diverse issues over the last few years, a diplomatic policy which appears to culminate the opening process initiated many years ago by Deng Xiao Ping.

The continuous efforts made by scholarship to provide an adequate answer to all these questions and their implications for the Chinese foreign policy and the international order itself might explain the current proliferation of publications aiming at analyzing different aspects of Chinese evolution and politics.

Thus together with more classical works giving account of the Chinese history like those of Buckley¹, Dardess² or Fenby³ and general works on China like those of Kissinger⁴ and Dillon⁵ among others, it is worth to mention scholars such as David Scott⁶ or Liselotte Odgaard⁷ who have authored a wide range of publications providing deep insights into the main features of China, its assets as well as its weaknesses. To that end, various dimensions of power are reviewed. These analyses are particularly useful as to assess Chinese likelihood to play a leading role in the next few years as well as the extent to which it will have to be considered a power with an important status in the international system. The contributions of Young Deng⁸, Guoli Liu⁹, Joseph S. Nye¹⁰, Gill Bates¹¹, Samuel Kim¹² or Harsh V. Pant¹³ might be mentioned at this point.

Besides, a great majority of publications have focused on the changes experienced by the Chinese foreign policy along with the links between those changes and the transformation experienced by the People's Republic of China in many other fields. In this point we should mention, for instance, the work of Andrew J. Nathan and

¹ Fenby, Jonathan *The Penguin history of modern China : the fall and rise of a great power, 1850-2008*, Penguin Books, London, 2008

² Dardess, John W. *Ming China, 1368-1644 : a concise history of a resilient empire*, Rowman& Littlefield, Lanham, 2012

³ Fenby, Jonathan *The Penguin history of modern China : the fall and rise of a great power, 1850-2008* Penguin Books, London, 2008

⁴ Henry Kissinger, *On China* Penguin Press, New York, 2011

⁵ Dillon, Michael *Contemporary China : an introduction*, Routledge, London, 2009

⁶ Scott, David *China Stands Up*, Routledge, Abingdom, 2007

⁷ Odgaard, Liselotte, *The Balance of Power in Asia-Pacific Security*, Routledge, Abingdom, 2007

⁸ Deng, Young y Wang, Fei-Ling *China: Power and Motivation in Chinese Foreign Policy*, Rowman and Littlefield, Oxford, 2005. See also Deng, Yong *China's Struggle for Status*, Cambridge University Press, Cambridge, 2008

⁹ Liu, Guoli *Chinese Foreign Policy in Transition*, Aldine de Gruyter, New York, 2004

¹⁰ Nye, Joseph "China's Re-emergence and the Future of the Asia-Pacific" in Liu, Guoli *Chinese Foreign Policy in Transition*, op. cit.

¹¹ Bates, Gill "Discussion of China: A responsible Great Power", *Journal of Contemporary China*, Vol 10 No 26 (2001) pp 27-32

¹² Kim, Samuel "China's Path to Great Power Status in the Globalization Era" in in Liu, Guoli *Chinese Foreign Policy in Transition*, op. cit.

¹³ Pant, Harsh *China's Rising Global Profile*, Sussex Academic Press, Eastbourne, 2011

Bruce Gilley¹⁴, who give account of the dynamics, changes and evolution of Chinese leadership. Likewise, albeit from a different perspective, we have to mention the efforts of Mark Leonard to review the different schools of thought and approaches to the different issues currently existing in China¹⁵. Finally, some of these scholarly works have thoroughly looked at the changes taking place in Chinese foreign policy as a result of the “opening” process undergone since the late seventies by the People’s Republic of China.

In this context, special attention should also be paid to Liselotte Odgaard¹⁶ for her scholarly contributions on the situation of security in Asia as well as the role played by the People’s Republic of China as regards security in Asia in general and the correlation of forces and the Regional Balance of Power in the area in particular. These approaches have conducted an in-depth analysis of the relations between China and some other powers in the region, notably, Japan and India. The work of Harsh V. Pant¹⁷ can be mentioned also in this point.

In connection with that, an increasing number of works aimed at analysing the rise of China, its specific understanding of its own national security and its impact on the global security have recently flourished. These works are meant to assess to what extent China is either an adversarial, revisionist power or a *statu quo* power. These are issues on which Western and Chinese approaches frequently differ. Prominent scholars such as Kevin J. Cooney, Yoichiro Sato¹⁸ or Russell Ong¹⁹ are to be noted for their contribution in this realm.

In a similar vein, from a perspective of Political Economy, Shaun Breslin²⁰, among others, has assessed the role and relevance of the People’s Republic of China in the Global Economy. He draws attention to the alternative economic model advanced for China and its impact on the relations between developing and developed countries²¹. Following this line of analysis, a number of academic works on the so called “Beijing Consensus” and its influence on Chinese Foreign Policy are worth mentioning here. That would be the case, for instance, of some works of Stephan Halper²² or Joshua Kurlantzick²³.

Also in connection with the Chinese understanding of its own security, a number of works provide useful insights into the Chinese approach to the human rights debate, their position as regards the US and European human rights policies and the widely shared view that Human Rights issues have been used by the West as an instrument to weaken the hegemonic position of China²⁴.

Likewise, it is worth mentioning the contribution of a number of works dedicated to the question of Chinese increasing interest in multilateralism, a field in which the input of Guoyuang Wu, Helen Landsdowne²⁵ and Michael Yahuda²⁶, among others, may be particularly remarkable. These scholars have made valuable attempts to explain how multilateralism, –and multipolarity–, have been seen by the PRC as a useful strategy to challenge US hegemony after the Cold War.

Finally, scholars such as Brzezinski²⁷, Sutter²⁸, Friedberg²⁹ and some others with different points of view and considering different sets of factors have tried to analyse the Chinese Foreign policy and how it conditions China’s relations with different areas and countries in the world, in particular with the US. In this context the likelihood for an eventual clash between the US and China in the future is assessed in some cases.

¹⁴ Nathan, Andrew J. and Gilley, Bruce *China’s New Rulers: the secret files*, The New York Review of Books, New York, 2002

¹⁵ Leonard, Mark *What does China Think?*, Harper Collins, London, 2008

¹⁶ Odgaard, Liselotte, *The Balance of Power in Asia-Pacific Security*, op. cit.

¹⁷ Pant, Harsh *China’s Rising Global Profile*, op. cit.

¹⁸ Cooney, Kevin J. and Sato (Eds) *The Rise of China and International Security: America and Asia Respond*, Routledge, Abingdom, 2009

¹⁹ Ong, Russell *China’s Security Interests in the 21st Century*, Routledge, Abingdom, 2007

²⁰ Breslin, Shaun, *China and the Global Political Economy*, Palgrave McMillan, Basingstoke, 2007

²¹ Peremboom Randall *China Modernizes: threat to the West or model for the rest?*, Oxford University Press, Oxford, 2007.

²² Halper, Stephan *The Beijing Consensus: legitimizing authoritarianism in our time*, Basic Books, New York, 2010

²³ Kurlantzick, Joshua *Charm offensive: How China’s Soft Power is transforming the world*, Caravan Books, New York, 2007

²⁴ Kim, Mingyoung “Political Construction of Human Rights” in Cooney, Kevin J. and Sato (Eds) *The Rise of China and International Security: America and Asia Respond*, op. cit.

²⁵ Wu, Guoyuang and Landsdowne, Helen (Eds.), *China turns to Multilateralism*, Routledge, Abingdom, 2008

²⁶ Yahuda, Michael “China’s multilateral and regional order” in Wu, Guoyuang and Landsdowne, Helen (Eds.), *China turns to Multilateralism*, op. cit

²⁷ Brzezinski, Zbigniew “Balancing the East, Upgrading the West”, *Foreign Affairs* 91 N° 1 January/February 2012

²⁸ Sutter, Robert G., *Chinese Foreign Relations: Power and Policy since the Cold War*, Rowman and Littlefield, Plymouth, 2012

²⁹ Friedberg, Aaron L. *A Contest for Supremacy*, Norton, New York, 2011

No doubt there are numerous publications dedicated to China-Europe relations where different aspects of the bilateral relation are addressed. In this fashion, they pay attention to the bilateral dialogue, the areas for agreement and disagreement, mutual perceptions, trade, investment, institutional and legal frameworks for cooperation and so on. As an example we can mention the works of David Kerr and Liu Fei³⁰, David Shambaugh³¹, Men Jing and G. Balducci, Nicola Cassarini, Robert S. Ross or Jens Hillebrand, among others.

In the aforementioned context, this book attempts to provide a slightly different perspective, looking at China's foreign policy from both the Chinese and the European standpoints. In other words this publication does not only provide a good account of the trends and characteristics of Chinese foreign policy but it also tries to illustrate the different understandings of the Chinese foreign policy actions embedded in both European and Chinese perceptions.

These different understandings are interesting in themselves but most importantly, they might set a solid basis for a joint effort to identify prospective opportunities for the reinforcement of China-EU cooperation while devising prospective areas where China-EU cooperation could be enhanced.

Thus, the book analyses the Chinese Foreign Policy by paying special attention to its goals and priorities, in particular regarding the Chinese approach to the different geographical areas in the world and the phenomenon of multilateralism and regionalism. Likewise, the Chinese position in respect to the different issues currently on the international agenda is also examined in detail.

This book constitutes an attempt to shed some light on the complexity and difficulties that the EU- China relationship might entail while showing up opportunities for cooperation for both actors.

The different chapters set the focus on a number of relevant issues that might have a decisive influence on the bloom or decline of the cooperation between China and the EU. The discussion gives the impression that, far from adopting a common stance, European and Chinese scholars have serious discrepancies regarding a number of fundamental aspects of international relations giving rise to some reasons for concern.

Nevertheless, the identification of those areas of disagreement and the enriching debate surrounding them are meant to serve well to the major purpose of the research project, which basically consist of fostering a more fruitful collaboration between China and the EU. In fact, the authors themselves seem to consider that there is some scope for greater cooperation between the EU and China.

The book is structured on the basis of nine chapters, illustrative of the growing importance of multilateralism and regionalism and the increasing interest in: the Chinese approach to those interaction patterns; the role and position of China in the framework of the Global Political Economy; the Chinese-EU relations, considering the China EU-Political Dialogue; the Chinese priorities in its relation with the EU; and the way the Chinese policy actions are perceived from the EU standpoint, both in the foreign policy and in the competition policy realms.

The first chapter prepared by Mario Telò presents a thorough analysis of the concept of multilateralism and the doctrinal debates that followed. In particular, it examines the crucial role that multilateralism has played over the last few decades and in recent times within the current complex and presumably multipolar international context.

This analysis is complemented by a comprehensive overview of the Chinese position in relation to multilateralism and multilateral initiatives displayed in recent times. The European perception of such approaches and the role China plays in them is subsequently examined.

The author goes beyond the formal analysis of the classic conceptions of multilateralism to provide an insightful conceptualisation of multilateralism as an effective tool for global governance. In this sense, Prof. Telò scrutinizes the conditions which such scenario would require. Among them, some concerns are raised regarding the necessary relaxation of Westphalian trends and dynamics, i.e. unipolarism, bilateralism and the balance of power. Similarly, some doubts are shed as to the introduction of changes aimed at ensuring that multilateral agreements are perceived as more efficient, legitimate and fair.

³⁰ Kerr, David and Fei, Liu (Eds.) *The International Politics of EU-China Relations*, OUP, Oxford, 2007

³¹ Shambaugh, David and Sandschneid, Eberhard *China-Europe relations : perceptions, policies and prospects*, Routledge, Abingdon, 2008

According to the author, multilateralism could emerge as a genuine system for global governance rather than an instrument for the maintenance of a Westphalian order. In this view, multilateralism must be understood in such a way that it may serve as a vehicle for a “multilevel collective transnational action” involving states as well as civil societies as truly leading actors in international relations .

In the second chapter, Juliet Lodge and Angela Carpenter draw on the example of China and explain how the EU approaches towards third states in a multilateral model of international relations might contribute to build up a common position of Member States within the EU.

Subsequently, these scholars examine a number of areas where cooperation between the EU and China has already taken place. In this sense, it is noted that in most scenarios there is still some scope for stronger cooperation between both actors. Not in vain, the authors support the claim that the EU and China have become more engaged as a consequence of both, their increasing cooperation as well as their shared interests in a number of fields.

All in all, the authors also remind us of the fact that the EU and China compete in the global market for oil, food and raw materials, a factor that might be worth considering in their relations. It is precisely on these sensitive areas where multilateral diplomacy is most advisable and advances in cooperation are particularly difficult to achieve. A good example illustrating this claim is the ‘arms embargo’ imposed by the EU upon China. This particular case, unlike an arms embargo in the traditional sense, constitutes an interruption of military cooperation and arms trade with China subject to non-binding differential approaches of each EU Member State.

The authors hold an optimistic view on the future prospects of EU-China relations and they consider that a strong case for increased cooperation can be build on the basis of shared motivations and interests. In particular, in an attempt to enhance both their regional and their global influence, it is foreseeable that the EU and China may skilfully resort to the tools of multilateral diplomacy to strengthen their position in the area. The dynamics of this relation might contribute to the establishment of standards across a broad range of activities and policy areas to the advantage of the enhancement of EU-China cooperation. This scenario might operate in areas where both actors share common interests. Some examples might refer to the fight against organized international crime, fraud, piracy and counterfeiting; the promotion of enhanced cooperation with other regional organisations or the collaboration in priority areas such as climate change and energy, health, migration, education and culture; or policy reform in the area of security. In particular, the cooperation between the EU and China in the design of future policies in some of these areas might be of great importance.

Likewise, the authors underline the significance of two main issues where the potential room for mutual cooperation might arise:

Firstly, support for socio-economic reform, sustainable development, good governance and the rule of law might be a motivating factor for cooperation. This area seems to have replaced capacity building and rural development programmes as the main goal of the EU in its cooperation with China.

In this regard, among the new priorities for EU funding, education, trade and investment, human rights and environment will have to be considered. In this sense they mention how cultural region-to-region and vertical and horizontal multilateral diplomacy allow the exchange of experiences. In other words, the resort to multilateral diplomacy and forums where multilateral negotiation and dialogue can be conducted may contribute to promote cooperation and mutual understanding.

Secondly, Juliet Lodge and Angela Carpenter stress that the EU integration process itself is a good example of how the strategy of multilateralism may be conducive to the achievement of goals in the domestic realm. This case might be of interest for China in its efforts to overcome the fragmentation of its internal market. A more unified Chinese market would of course benefit China’s economic development, but it would also be highly beneficial for EU-China trade and business relations, as China’s fragmented market is frequently the cause of difficulties and misunderstandings in their relationship.

In Chapter 3 Maria-Eugenia Bardaro and Frederik Ponjaert, with a clearly innovative approach, and departing from more traditional analysis of Chinese foreign policy towards the Asian region, assess the extent to which we can consider that the PRC has managed to develop a specific approach to regional affairs where regionalism

and multilateralism constitute crucial aspects of the EU-China relations. Maria-Eugenia Bardaro and Frederik Ponjaert also examine to what extent we can consider that the PRC has indeed given rise to its own “Neighbourhood Policy” or an “Asian Neighbourhood Policy”.

The authors unveil the commonly mistaken assumptions underpinning most constructions of EU’s and China’s relations as comparable scenarios. Assuming that China is actually developing a coherent regional approach comparable to the European Neighbourhood Policy, the milestones and methods of both strategies may be similar. Nevertheless, their underlying models and implications are clearly different in the actual practice.

The European Neighbourhood Policy (hereinafter, the ENP) constitutes a clear example of these conceptual clashes. From the authors’ viewpoint, this policy was created as the result of a single multilateral effort on behalf of the EU Member States to include all their immediate neighbouring countries under a common frame so as to consider them as a single partner region. According to these scholars, this neighbouring policy was set up in a clear attempt to protect itself from external threats and regardless of region-building concerns.

In contrast to the EU position, China seems to have developed a very different approach which takes good account of the differences between its peripheries. All those differences together with its own strategic interests and goals as a rising power have been the defining elements in its strategy.

The EU, through its ENP, seems to have forgotten its initial interests in region-building and even its multilateral appeals, but China’s changing neighbourhoods might have provided an unparalleled opportunity to test and develop its own multilateral principles, which no doubt may have an impact on the East Asian reality.

In other words, whereas EU’s neighbourhood policies seem to be conceived as an efficient functional problem-solving tool, China’s diverse experiences of multilateralism in its neighbourhood give the impression of an instrumental, strategic approach to multilateralism with domestic, regional and global implications. The authors consider that “*Neighbourhood*” may well have been a testing-ground for multilateral functional governance, whereas China has found in its neighbouring regions a good area to test its geo-strategic approach towards multilateralism.

In Chapters 4 and 5 Chinese goals and priorities in economic and political terms are analysed from a Chinese point of view. Thus the chapters provide a valuable contribution as long as they permit to confront the Chinese view of their own goals in the economic and political fields with more commonly found Western analysis of these issues.

In particular, Chinese priorities and approaches to foreign relations constitute the focus of the fourth chapter, written by Xinning Song and Weiping Huang.

In this chapter, the authors outline the main characteristics of Chinese Foreign Policy under Hu Jintao, paying special attention to the different cases of developed countries, neighbouring countries and developing countries are examined.

Further, Xinning Song and Weiping Huang explain in the chapter the main conditions for a harmonious world, one of the supposed goals of Chinese Foreign Policy. In their opinion, two key words and five main elements should be present for that situation to emerge:

Those two key words are lasting peace and common prosperity.

Those five elements would be:

- (1) Politically, all countries should respect one another and conduct consultations on an equal footing in a common endeavour to promote democracy in international relations.
- (2) Economically, they should cooperate with one another; draw on one another’s strengths and work together to advance economic globalization in the direction of balanced development, shared benefits and win-win progress.
- (3) Culturally, they should learn from one another in the spirit of seeking common ground while shelving differences, respect the diversity of the world, and make joint efforts to advance human civilization.

(4) In the area of security, they should trust one another, strengthen cooperation, settle international disputes by peaceful means rather than by war, and work together to safeguard peace and stability in the world.

(5) On non-traditional security issues such as energy and climate change, they should assist and cooperate with one another in conservation efforts to take good care of the Earth, the only home of human beings.

Subsequently, these scholars look at the strategy and the tools set forth by the Chinese leadership to implement their foreign policy. This section continues with the analysis of China's role as a responsible power, the question of multilateralism and the importance of keeping a low profile stance. Next, the authors address the issue of the different understandings of multilateralism in both China and Europe, a topic dealt with throughout the book. In this regard, they explain how China considers multilateralism as a kind of inter-governmental arrangement useful to deal with common issues. In the context of the multilateral framework, all the sovereign states are equal to one another and the non-intervention in other's internal affairs principle is considered as the organizing principle, as the cornerstone. In this sense, China regards multilateralism as a diplomatic tool rather than a mechanism for the management of the international order. This conception of multilateralism is better understood if we take into account that the term "multilateral diplomacy" is frequently deployed in China.

Further, the authors continue to analyse the decisions China has made in its foreign policy and how these choices may determine the different levels of its foreign relations.

Last but not least, the chapter also analyses the Chinese Strategy for Economic Development, Chinese economic relations with both the US and the EU and the difficult question of the exchange rate of RMB.

In Chapter 5 Zhimin Chen, Bingran Dai, Zhongqi Pan and Chun Ding explore China's Priorities and Strategy in the sino-EU cooperation. Looking at the issue from the standpoint of the PRC, the authors reassess both the evolution of the European process itself and the evolution of the relations between China and the EU. On this basis, they highlight the difficulties encountered as a result of the disappointment following their strategic partnership and the unfulfilled potential of their relations. Thus, although the authors are aware that dramatic changes might not happen in the relationship overnight, particularly in the sensitive current context, they also agree on the need to develop their relations further. In fact, some opportunities to strengthen their links might arise in future scenarios.

They conclude the chapter with an analysis of the Chinese priorities in the relation with the EU in the near future with a special focus on the ways in which these relation might be better protected in the context of the new EU foreign policy framework. In this sense, they defend a pragmatic approach according to which China might have to deal simultaneously with the EU as a single actor on a bilateral basis, and with the different Member States at a multilateral level. Nonetheless, they remain optimistic as regards the future prospects of the relationship in the short run.

In contrast with this analysis of Chinese policies and goals from the Chinese point of view, in Chapter 6 Fernando Delage and Gracia Abad explain how Chinese approaches, actions and goals are perceived from the EU. The authors do not simply review Chinese policies from a European point of view as it is frequently done, but they analyse European perceptions of Chinese foreign policy.

Within this chapter would sound better, they give good account of the significant implications that China's policies may have for the current international order structure and governance, with special emphasis on the opportunities for cooperation arising from that situation. In this light, they explain how China's decision to join the international community has brought along some changes and challenges for the existing order but, at the same time, it has allowed China to be considered as one of the crucial actors in the globalisation process.

To a large extent, the impact of China's rise on the global trade system is the result of a combination of multiple factors among which we can mention China's exports, outflow investment, foreign aid policies and loans as well as its growing domestic demand. Likewise its growth pace and, consequently, its increasing consumption of energy and raw materials are influencing the prices and the access to these resources. These growing needs are undeniably the base for many Chinese Foreign Policy Actions and trends.

Most interestingly, these factors may explain why some reasons for concern might still remain in the current context, at least as it is perceived from an European standpoint. Thus, the EU resents what it considers as unfair competition in terms of labour and safety standards as well as protection of intellectual property rights, important aspects for Chinese and European “competitiveness” in the global markets. Finally, European governments are increasingly concerned with the growing trade deficit with China.

Similarly, the EU harbours the concern that China’s rise might become a major challenge to the EU’s social and economic model, already questioned as a consequence of the global economic and financial crisis which is having a particularly serious effect on the Euro zone.

Moreover, China’s growing presence in third world regions, notably Africa, constitutes an important cause of unrest for the EU, as this position threatens Europe’s traditional role as their main partner. This may not only confront EU economic interests but also weaken its ambitions as a global actor as well as its ability to promote its own values through its foreign policy.

The reform of the global governance architecture is another field to which the EU attaches great importance. The EU is also convinced that China, which is becoming a key actor in the world stage, might be a good partner in this realm.

However, the extent to which the EU and China share their goals as far as the reform of the global governance architecture is concerned remains an issue to be pondered in the future. To put it simply, it is far from clear if both, the EU and China, share the same expectations about global governance institutions.

The origin of many disagreements, as the authors explain, is likely to lie in the different stances that the EU and China have on foreign policy issues. Whereas China’s approach is predominantly realist, the EU maintains a liberal approach with elements of both institutionalism and idealism which may help to understand its normative approach as a global actor. These different conceptions may result in a contrasting situation where Europeans prefer a world shaped by institutions and rules managed through multilateral governance whereas the Chinese favour an international system based on the balance of power and the creation of a multipolar international order. These conceptual differences have given rise to a series of points of friction in the bilateral relationship, as Delage and Abad put forward.

All in all, the authors argue that even though the relationship between China and the United States might be considered as the most important geopolitical relationship of the 21st century because of their economic power and probable strategic competition, the China-EU relationship may be crucial as well. The consequences of these dynamics are various: should China and the EU manage to develop a friendly and productive strategic partnership, they would contribute positively to the emergence of a world where multilateral governance would become increasingly important, but if their relation becomes frosty, the scenario of competing blocks would become most likely.

In Chapter 7 Justo Corti and Alicia Sorroza revisit the relations between the European Union and China paying special attention to the most relevant aspect to take into account: the twofold approach to the EU and its institutions as a single international actor and, simultaneously, to the the EU Member States.

Along these lines, the authors examine the main channel through which the EU and China are meant to develop a firm and fruitful relation: the EU-China Political Dialogue and the efforts to build a strategic partnership.

Subsequently, the authors assess the contribution that the EU-China political dialogue has made in some specific fields, such as of the closely related issues of environment, energy and climate change. Achievements as well as shortcomings are identified in this analysis.

Similarly, Alicia Sorroza and Justo Corti conduct a thorough assessment on the impact that the global financial crisis and its effects on the Eurozone have had on the relation between the EU and China.

The authors explain with concern that although examples of effective cooperation between China and the EU are numerous, there are still some clashing points of view and contested issues in some areas.

In particular, the ability of the EU to influence Chinese domestic or international policies is far from being clear. In fact, the leading role of China in the global economy (including trade and investment flows) could not be considered as a consequence of EU policies or desires but rather, as a consequence of China's successful economic hegemony.

In line with some other contributors in this book, Justo Corti and Alicia Sorroza support that trade and economic issues are probably the main aspect in which the EU may convey certain power and influence. In the rest of areas, even in environmental matters, the EU seems to have been losing leadership over the last few years.

In Chapter 8 Enrique Fanjul focuses on a particular aspect of EU-China relations: trade relations and business cooperation. The author scrutinize the issues that should be given priority along with the aspects that should be overturned, if commercial and business relations are to be enhanced.

Accordingly, Enrique Fanjul examines the context in which trade and business relations with China are conducted, paying special attention to the uncertainties that foreign companies have to endure in China. These uncertainties which may be at the root of some observable changes in the pattern of Chinese economic growth, might end up generating tensions in bilateral trade

Thus, Enrique Fanjul highlights the importance of some sensitive issues within the realm of trade and business relations and stresses the convenience of developing a constructive dialogue on these areas. The disagreements regarding the exchange rate of the Chinese currency or the resort to dumping strategies constitute two examples of these contested issues.

Another problematic question concerns the access to the Chinese market. Despite the existence of numerous obstacles, the author remains optimistic regarding the prospects for future relations.

This chapter concludes with the identification of some areas for further cooperation and some recommendations for the improvement of current relations as far as trade relations and business cooperation are concerned.

Finally, in Chapter 9 Jerónimo Maillo examines another specific issue carrying significant weight in the relations between China and the EU which nonetheless is not very frequently analysed in detail: the Chinese Competition Law and Policy. Special attention is paid to the recent Chinese Antimonopoly Act, which came into force in 2008.

The author looks at the evolution of Chinese merger control regulation as a clear example of recent developments in Chinese Competition Law. In particular, he argues that, as a result of the effective enforcement of merger regulations carried out by Chinese competition authorities, this country is becoming a strategic jurisdiction as regards the choice of the forum to set up business concentrations. Accordingly, it is claimed that China cannot be considered as a negligible actor in the current context of Global Competition policy, especially in the area of Merger Control. Likewise, Jerónimo Maillo considers extremely important to enhance international cooperation with the Chinese authorities in order to provide them with technical assistance to ensure a robust enforcement system. Given the increasingly significant expansion of the Chinese market share worldwide, all these efforts to secure a solid, transparent, legally certain and non-discriminatory merger control system may, in return, feed back into the global economy bringing further benefits for the international community.

Jerónimo Maillo continues his analysis by examining the empirical data concerning the implementation of Chinese merger regulations. He highlights some curious trends operating in the Chinese context. On the one hand, although it is obvious that enforcement is getting stronger -as proven by the fact that certain acquisitions have been blocked out-, in the great majority of cases, Chinese authorities show a compelling preference to negotiate with the undertakings rather than resort to strict prohibition. On the other hand, the author considers that despite the fact that Chinese authorities are becoming increasingly efficient in the management of the workload, as cases are decided in shorter lapses of time, there is still some room for improvement.

Explicitly, the author shows some reasons for concern within the realm of concentrations, in which transparency shall be clearly improved by Chinese authorities. In this regard, the enactment of more detailed guidelines might be highly recommended, in particular in connection with the Chinese Anti-monopoly Law (AML).

Finally, the author raises the issue about the neutrality of Chinese merger control decisions. Here, concerns may not be exaggerated if we consider the unequal enforcement of merger regulation, i.e. the stricter supervision of foreign concentrations compared to a more lenient implementation in local mergers. Similarly, it is not clear if

competition laws and compliance standards are equally implemented in the case of state owned and privately owned companies.

Many scholars claim that Chinese competition authorities take into account not only competition concerns but also issues such as the 'development of national economy' or 'national (economic) security' in their decisions. Of course, Chinese authorities insist on their neutrality and stress the fact that they are making serious efforts to ease these concerns. Nevertheless, stronger commitment to enhance transparency is necessary for concerns to fade away. As Mr. Maillo concludes, this is not a minor issue for Chinese merger control system, as it may have a clear impact on its credibility.

This book constitutes the final result of an international research project, in which researchers from a wide variety of disciplines have been engaged for more than two years. This project has been supported by the European Commission and it was led by the European Studies Institute of San Pablo CEU University (Madrid) in collaboration with other Centres of Excellence from both Europe (IEE – *Université Libre de Bruxelles* and JMECE – University of Leeds) and China (CESRUC - Renmin University of Beijing and CES - Fudan University of Shanghai).

Apart from reputed scholars coming from the universities mentioned, experts from other public institutions in China and Europe have also contributed to this research. Among the Chinese institutions, it is worth mentioning the Academy of Social Sciences, Shandong University, Shanxi University, Zhejiang University, Beijing International Studies University and the University of Macau. In Europe, insightful contributions have been incorporated from Essex University, Egmont, University of Trento or the Hungarian Academy of Sciences. Last but not least, American leading scholars like David Shambaugh from George Washington University have also made valuable contributions.

In this context, a series of international events were organised in order to enhance collaboration and the exchange of views among the contributors of this book. An initial meeting was held in Brussels, two international conferences took place in Beijing and Chengdu in 2010 and in Madrid in 2011. Finally, two PALMs –one in Brussels and another in Leeds–, both in 2011, were held to present their findings and take useful inputs from the academic community on the different issues covered in this project.

All along the project, there has also been close collaboration with Spanish and Chinese public authorities and dignitaries. Notably, the first conference in Beijing was attended by Wang Hongjian, Deputy Director-general for European Affairs of the Chinese Foreign Affairs Ministry. Likewise, the Deputy General Director for Asia of the Spanish Ministry of Foreign Affairs took part in the second conference celebrated in Madrid. Finally, this project has benefited from the views of private companies with interests in EU-China relations.

Overall, the book is the result of close collaboration between the EU and China to assess the state of their relationship and their agreements and disagreements while identifying areas for improvement. In this sense, the book may be a good starting point.

Chapter 1

Multilateralism and global governance: a challenge for EU and China

Mario Telò

This paper aims to provide both a theoretical and historical background regarding the concept of, and theoretical debate about, multilateralism and an analysis of perspectives concerning a new multilateralism for the 21st Century. It will cover, on the one hand, the many gaps of the multilateral legacy of the past six decades and, on the other, the new challenges of regional and global cooperation within an emergent, asymmetric, heterogeneous and multipolar world, where not only the European Union and the US but also the BRICS and notably China mention with evidence, even if with distinctive understanding, this concept as a key word of their international policies.

1. Multilateral cooperation: conceptual definition and history

Multilateralism has been defined in wider and narrower ways. According to Robert O. Keohane it is an 'institutionalized collective action by an inclusively determined set of independent states'; it is also defined as a 'persistent sets of rules that constrain activity, shape expectations and prescribe roles'¹. According to John G. Ruggie, 'multilateralism is an institutional form that coordinates relations among three or more states on the basis of generalized principles of conduct...'². The minimum requirement (the number of club members) is very relevant when looking at multilateral arrangements from an historical point of view. Multilateral agreements, regimes and organizations emerge in the 19th century and consolidate their role despite the failures and tragedies of the violent first half of the so called 'short century' (the 20th) because a number of states, notably the European states, are interested in increasing cooperation.

Research on multilateralism has had to take into account the challenge of the realist and neo-realist theoretical questioning, emphasizing competition among states, wars, protectionism and anarchy. How does multilateral cooperation interact with the self-interest of states? Several realist approaches even argue for dyadic cooperation.

However, critics question the realist approach on two fronts:

- Under certain conditions, the theory of the state of nature, and game theory as well, views the rational self-interest of an autonomous state as a sufficient background for a contractual relationship with one or more other states: repeated game, side payments, negotiation in the longer run, may allow for an explanation of bilateral cooperation. However, a deepening of multilateral arrangements needs more preconditions in addition to self-interest: a certain degree of reciprocal trust, reputation, the support of domestic economic and non-economic demands, ideas and common aims of states, in some cases, a shared perception regarding external threats, extended state cooperation not tied to specific short term gains but based on mid- to long-term promises, states' goodwill including the acceptance of a limiting and/or sharing of national sovereignty.

- Multilateral arrangements highlight the classical security dilemma. The way out of anarchy is based on the various concepts of collective security, security with the other and not against the other, and the indivisibility of peace. This is not only the case of the UN but also of security communities such as the EU or MERCOSUR. Even in the case of the NATO alliance, the basic principle of ‘all for one’ plays a crucial role.

In this section we will try to explore the historical roots of multilateralism in the controversial and contradictory civilization process of multipolar international relations. The history of multilateralism offers examples of routes away from anarchy, beginning with bilateral arrangements, and then with an increasingly institutionalized multilateral setting of international relations. In some of its historical versions, the multipolar balance of power is incompatible with anarchy. Multilateralism can be both institutionalized and informal, legally founded or only politically founded. Multipolarism can be based on conflicting state interests or understood as aiming at some form of co-operation and convergence among states. In some cases multipolar orders included common objectives such as stability and/or peace. Building a ‘security complex’ including one’s enemies (the North–East Asian Security Complex and the emerging East Asia Security Complex³), and even opposing alliances (such as NATO or the Warsaw Pact), may be considered a first step away from anarchy. The 19th Century European Concert was a clear example of the regulating of interstate conflict by conference diplomacy. Already Metternich conceived the European Concert as oriented towards stability and peace (albeit in his reactionary understanding). Later on, during the *Belle Époque*, 1871–1914, the European multipolar balance of power did offer a framework for the development of the first civilian multilateral arrangements. We fully understand that, seen from a non–European point of view, notably from a Chinese point of view, the European Concert looks like the cradle of colonialism and imperialism, in Africa, America and Asia, including in China at the beginning of the 20th Century. However, the highly contradictory *Belle Époque* also provided forty–five years of liberal peace and stability within Europe, was the context of the first civilian multilateral agreements regarding mail, measures and weights and so on and of the first wave of liberalizing of multilateral trade under the UK hegemony. The political struggle between liberal multilateralists and imperialists marked several domestic political spheres during these decades. We think that, in spite of the breakdown of this trend towards a civilizing sovereignty during the ‘Thirty Years War’ between 1914–1945, this European multilateral legacy was important, and still matters.

However, it is true that the history of European multilateralism and its relationship with multipolarism is controversial and that the revived European multilateralism after 1945 was essentially based on US pressures (the Marshall Plan and the OEEC) following the failure of the previous European state system. All in all, the current routinized multilateral intergovernmental relations, the set of regimes that distinguishes the EU co-operation system among member states (European Council and Council of Ministers) is also the legacy of a *longue durée* process which emerged during several centuries, before the era of American hegemonic stability. The deepening and broadening of European regional multilateralism in a post–hegemonic context strengthens the need for this kind of *longue durée* approach.

The gradual process of civilization of state sovereignties had already started in the 15th and 16th centuries among the Italian small states and was Europeanized and definitely set in motion by the Westphalian Treaty (1648) and continued over three centuries until the final breakdown of the European Concert. The political principle which explains the roots of this ‘European states society’ (F. Chabod⁴) became explicit only with the Wilsonian (1919) and Rooseveltian (Bretton Woods Conference) idea of American international multilateralism (Ruggie⁵). Already prior to this, and for several centuries, the balance of power had no longer been an occasional alliance, but a project both theorized and consciously sought by state leaders as a principle of political action. What is the historical context of this? It happened after the crisis of the *Respublica Christiana* and the end of Middle Ages, in secularized Europe, when religion began to be a political instrument of independent national sovereigns. Modern diplomacy develops in the context of the mutual recognition of treaties, of borders, and the new habit of choosing a third party as referee and warrant of bilateral treaty implementation; and, last but not least, the system of ‘*copartagéant*’, limiting, on behalf of the balance of power, the minor states’ sovereignty. Stanley Hoffmann in his early book (1961) stressed the continuity between such an initial step of reciprocal recognition between states (beyond anarchy) and the highest step of international law developing towards a ‘community law’⁶.

The literature is in agreement that for a properly working ‘balance of power’ the main (around five) actors must be similar, insomuch as their economic and military power is concerned. In the past a system of the balance of power could exist thanks to a kind of hegemonic power. It is a matter of fact that in the 18th and 19th Centuries,

England increasingly became the 'holder of the balance' of a dynamic, multipolar, inclusive balance of power system, which, in spite of the 25 years 'revolutionary system' (1789–1915, S. Hoffmann), and its conservative features, was able to adjust to change and eventually to integrate new emerging powers such as Russia, Germany and Italy. The historian F. Chabod emphasises that such a system of states was 'interdependent' while 'articulated', and despite the division between states, politically united on the principle of the balance of power, the symbol of the recognition of the states' common interests, as a kind of European *international distinctive identity*⁷. It was also the background for a kind of common rule for states' behaviour, a political norm of action including diplomacy and war (and *jus in bello*). Combining unity and diversity was indeed the distinctive principle of European civilization, when compared with other continents; it is rooted in the common cultural background provided by both the Renaissance and the Enlightenment. It was in contrast to Europe of the Middle Ages on the one hand, and to non-Europeans, on the other, in two ways, first because nowhere had inter-state relations evolved in that way, and second, because of its colonial and imperialist relations with other continents.

H. Kissinger's idealized picture of the European Concert of the 19th century ignores the evidence of such a combination of a setting of internal peace and the destabilizing global 'age of empires'⁸. However, in the 19th century the Concert of Europe carried out similar functions to those performed by current soft international organizations, 'providing access to decision making by states not directly involved in a conflict, offering assurance to members about each others' intentions, and requiring conformity to shared norms as a condition for acceptance as a member in a good standing'⁹.

Secondly, how does one explain the first multilateral arrangements regarding civilian issues, what D. Mitrany calls the specific 'common interest', for example the International Telegraph Union in 1865, without taking into account such a co-operative kind of multipolarism? This was the most significant of a series of significant multilateral arrangements¹⁰. Mitrany is wrong in contrasting functional cooperation with intergovernmental regimes, which are really two sides of the same coin. Multilateral cooperation and the central role of the British Pound (the *Gold Standard*) are some of the main pillars of the so called '*Pax Britannica*', the instruments of the international system which has been defined by some scholar as a British hegemonic stability¹¹, in the 19th century and, thanks to the illusory Washington treaty of 1922, again after WW1, until its final breakdown in August 1931¹².

It is relevant for understanding the background of the current pluralist international trade system that multilateralism was not the only principle of international trade at that time. For example, the process leading to the German *Zollverein* (1834), and the Anglo-French commercial treaty (1860) were based on bilateral arrangements provoking, by domino-effect, trade liberalization¹³. In spite of the conflict with German (and other powers') protectionism, the British liberal multilateralism was a way of stabilizing and adjusting the system of balance of power, even if it eventually proved incapable of managing the emergence of Germany as a power within the system.

Complementary interpretations also suggest a bottom-up emergence of multilateral cooperation in Europe at the middle of the 19th century, thanks to the spilling-over of domestic codification of universally constraining norms, from national to international life¹⁴. However heterogeneous and pluralistic the international system may have been between the 19th and early 20th Centuries, the British-led multilateral system and the multipolar European states system both ended at the very same epoch, that is between the two world wars, in the context of what I. Wallerstein calls the European 'Second Thirty Years War'.

This was an historical turning point. It is maybe true that the emerging global actors and specifically the two superpowers were partly dependent on European culture. However, what is certain is that Europe was no longer the world's centre. The main actors of classical multipolarism itself, namely the Great Powers of the 19th Century, were declining and Europe's relative weight within the international system reducing, even if Europe still typically has a bridge-making capacity with any part of the world.

However, the new epoch of European US-led multilateralism did not start from zero. European multilateralism was not re-born only because of the new US hegemony after 1944/45. How does one explain the huge difference between the type of US hegemony in Western Europe after WW2 and in East Asia –where regional multilateralism was not even sought by US– and the bilateralism that characterized the new relationships with Japan, Southern Korea, Singapore, Taiwan, Philippines etc.? The rebirth of economic and political multilateralism in 1944–47

was already happening in Europe before the beginning of the Cold War (1947): the Bretton Woods conference on the monetary system, the IMF, the World Bank, in 1945 the UN, in 1947 the GATT and the 'Marshall Plan' (with the 16 member Organization for European Economic Cooperation). Even when global multilateral options (the UN Security Council) are prevented by the emergent bipolar threat and resulting new power hierarchies, multilateral security remains US-centred as far as Western Europe is concerned (i.e. NATO).

It would be impossible to explain this distinctive feature of US hegemony in Western Europe without taking into account the European political history mentioned above. Implementing and deepening multilateralism, according to the federal/functionalist view of the grounding fathers of European unity, was consistent with internal demands arising from civil society, with endogenous factors and rule-making, rooted in modern history, all of which in a relationship of both continuity and discontinuity with the controversial vicissitudes of the European state system. Of course, within the new international system born in 1944–47, what used to be obvious during the centuries of the Westphalian European state system became increasingly problematic, that is the identification between infra-European order and global order.

Realists would argue that the Western and European multilateral institutions would have been inconceivable without the bipolar nuclear confrontation, which, in Europe, meant longstanding US leadership¹⁵. However, the strength of European continental political culture made the balance between new global US-led and regional multilateralism a controversial issue from the very beginning. For example, the division between the UK-led EFTA (1960) and the 6 EC members (Treaties of Paris, 1950, and of Rome, 1957) resulted out of two very diverging concepts of multilateralism, both compatible with US hegemony, but only the second of the two included deeper integration and supranational institutions. US tolerated EC trade and agrarian protectionism, as well as national Keynesian policies, for decades because of both strategic (anti-USSR) reasons and its commitment to the internal social stability of the allies¹⁶. GATT Art. 24 (transferred to the WTO art 24) appears to be a soft compromise framework for a real problem, which by 2006 is still largely unresolved: on the one hand, the widening to 27 members of the EC-EU shows that the model of deeper integration has won the competition with the current 4 member-state EFTA, but on the other hand the external and internal pressures for an EFTA-style type of European multilateralism have been greatly increased by both enlargement and globalization.

In conclusion, in a narrow sense, multilateralism can be seen as an instrumental tool, successively subordinated to the European multipolar balance of power and to the bipolar confrontation after WW2. However, multilateralism is an expression of long-term dynamics of civilization of the relations among states, increasing civilian and sequential exchanges. Multipolarism and multilateralism are distinct and to some extent conflicting concepts, even if we have shown that they are somewhat linked in modern European history: both are in opposition to unipolar/unilateralism, on the one hand, and an anarchical international system on the other.

The culture of multilateral cooperation is deeply rooted in Europe; as opposed to the hard versions of the balance of power, it can be considered as a form of implementing the political principle of state cooperation. In our opinion, these historical roots and the link between internal experiences largely explains the asserted European interest in global multilateral cooperation, diplomatic conflict prevention and crisis management, its interest in post-war reconstruction and the distinctive European 'tradition of making a political analysis of conflict, pragmatically looking for compromises'¹⁷.

2. The challenge of an emerging multipolar world

The emergence of the new Asian economies is challenging the European Union to adapt its multilateralism to a changing world, whose axis is shifting eastwards. Markets for goods and services and growing Asian pro-capita income pose a range of opportunities for the European exchange system. Asian technology powered economy and its buyout of some ICT is up-ending the supply chain and value creation. Asian demographic trends are complementary to the European one and may provide an increasingly educated labour force. Contrary to the first three rounds of globalization (ancient times; European empires; and US hegemony) we do share a consciousness of common global challenges: in terms of financial architecture, climate change, poverty, peace, Europe is no longer at the centre and risk becoming marginal in a world where the axis is moving towards the Pacific. Eurocentric thought is over. As an example we can quote G. W. F. Hegel, the most important German philosopher: 'Universal history moves from East toward West, because Europe is really the end of history, whereas Asia is her beginning'¹⁸. It is not difficult to find the roots of this great Eurocentric idea in a broad stream

of political thought from ancient Greece (Xenophones and Plutarch), to Machiavelli and Montesquieu, Voltaire and Kant: the idea of Europe as a place of freedom and individual liberties versus a collectivist and authoritarian Asia. What about the impact of the dramatic change which is occurring in economic interdependence and in the redistribution of economic power, demography, and social development, on the structure of the 21st Century world?

What kind of multipolar world is about to emerge? By multipolarity we may understand two different tendencies: either the less important descriptive fact that the distribution of powers shift from one or two to several centres, or a conceptual framework for a new international system –a world system where only the balance of nuclear and military power can prevent war. Several comments mention the old European system of 5–6 great powers (changing as far as its composition is concerned), which stabilized Europe, though challenges and wars, between 1648 and 1914. Is such a ‘back to the future’ scenario likely to occur at a global level?

Despite the relevance of power–politics in Central Asia, East Asia, South Asia and North–east Asia, national powers do not entirely share the traditional multipolar, power politics agenda. On the one hand, the world is witnessing not only local crises but the strongest threats to peace and to stability. On the other hand, there is much evidence of the emergence of a highly asymmetrical multipolar world, where a classical balance of power logic does not work because of the diverse and changing nature of each participating power (India, China, Japan, Iran, Russia, the US).

First, there is and will remain a structural and increasing gap between the military and nuclear power of EU/ India/China on the one hand, and of the US on the other. Second, Chinese, Japanese and Indian defence budgets are still substantially smaller than that of the US and also of France and the UK.

Table 1 regarding the top military spenders in 2008 (SIPRI Report 2009)

Rank	Country	(\$ b.)	Share (%)
1	USA	607	41.5
2	China	[84.9]	[5.8]
3	France	65.7	4.5
4	UK	65.3	4.5
5	Russia	[58.6]	[4.0]
6	Germany	46.8	3.2
7	Japan	46.3	3.2
8	Italy	40,6	2.8
9	Saudi Arabia	38.2	2.6
10	India	30.0	2.1
World total		1464	

NB [] = SIPRI estimate 2009. The spending figures are in current US dollars. The 10 biggest spenders in 2008 are the same as in 2007, although some rankings have changed. In particular, in 2008 China was for the first time the world’s second highest military spender and France narrowly overtook the UK.

After looking at the SIPRI report, the question which should be addressed is that of the quality of multipolarism. Is a kind of an enlarged and new society of great powers (for example, through an extension of the G8 or UNSC, for example) sufficient as a background for a new kind of multilateral cooperation, beyond mere instrumentalism, ‘free rider’ practices, the logic of power, and a rhapsodic implementation of multilateralism as a ‘consumption good’?

The current international economic crisis offers opportunity for the return of political choice, both at domestic and global levels. Does this mean the return of a narrow understanding of multilateralism, enhancing national sovereignty, both as its internal and external dimensions are concerned? Several facts suggest prudence in terms of this conclusion:

- the asymmetrical primacy of the US (according to the SIPRI report 2008, the US alone is spending in 2007 for its military budget more than the next 10 powers and ten times more than China).
- the evident heterogeneity of the five to six major powers (USA, Russia, India, China, Japan, UE, Brazil);
- the continuing influence of the multilateral network and of complex interdependence, where incentives for participation are based on reduction of transaction costs, cost–benefit calculations, etc.;
- the nature of global challenges favouring multilateral cooperation for the common good, beyond a narrow understating of reciprocity: climate change, financial instability, poverty of the ‘Bottom Billion’, terrorism, etc. (with their huge respective implications for comprehensive security) – military power is not the best means to address such threats.
- the evidence of a growing linkage between the internal and external dimension of policies and policy cooperation, suggesting a deeper understanding of international cooperation, beyond a narrow understanding of rational choice and closer to the ‘social exchange’ model.

3. East Asian cooperation and the European perception of China’s multilateral approach

The emergence of a multifaceted East–Asian multilateralism is an extraordinary innovation of the last twenty years. The end of the cold war has fostered already–existing tendencies rooted in traditional regional ties, whose roots in turn can be found in the pre–colonial fiscal system surrounding China and including many of the current members of ASEAN. A large literature already exists underlining the long term evolution and the perspective of development of multilateral cooperation in East Asia. Every state of the region has its own multilateral approach conditioned by national culture, regime and economic strength. However a multilateral, multilevel, multi–actor architecture of regional and global cooperation is already framing East Asia and will shape the international relations of the 21st Century¹⁹.

Let us start by evaluating the framework of the East Asian changes now occurring. The economic crisis may bring further regional cooperation or a growing risk of increased traditional and new conflicts in this economically decisive region. Asia is still characterized by both inter–state and internal uncertainties.

On the one hand, the international context is the most unstable in the world, because of both local and major unsettled disputes (Iran, Afghanistan, Iraq, Kashmir, the Korean peninsula, China– Japan relations). With regard to internal uncertainties, there is no doubt that with the exception of Japan, and to some extent South Korea, East Asia is still characterized by extensive internal uncertainties and the potential instability of young democracies or centralized political systems. Even democratic Japan has not yet had a mature experience of alternating centre–right wing and centre–left wing national governments. These factors suggest prudence and that the future will be unpredictable.

On the other hand, the extraordinary Asian economic and trade development occurs in a situation where there is a competition of two currencies (yen and yuan) for regional leadership which is still undecided and will be not be easily settled in the coming decade. However, what is new is that both bilateral cooperation and regional multilateralism are not only growing up –thanks to ASEAN and its capacity of inclusion, in several circles, of the other countries of the region– but that ‘asianization’ is going to be strengthened. Compared with the time of the APEC hegemony, internal Asian pressures are more significant. ASEAN remains in the driving seat: ASEAN plus 1 (FTA with China before 2010 and 2015), ASEAN plus 3 (China, Japan and S. Korea), plus 6 (plus India, Australia and New Zealand), and the Asian Regional Forum (ARE, inviting EU, US and non–Asian powers to discuss once a year sensitive security issues). Furthermore, China has been able to establish the Shanghai Cooperation Organization with its secretariat in Beijing (SCO) and is leading the six–party talks regarding the Korean peninsula. Nobody expected such a development twenty years ago.

Are the foundations of Chinese multilateral cooperation strong enough to realistically allow us to rely on its commitment to multilateral cooperation?²⁰ On the one hand, the Chinese cooperative approach looks to be structural and long–term. The evolution of the external economic relations and foreign policy of the People’s Republic of China has been combining, for several decades already, in a distinctive way, Chinese national interests and bilateral/multilateral cooperation. We can categorise the PRC’s external relations in four successive epochs.

1. In the first epoch, from 1949 to 1971, Chinese isolation in the context of US containment policy and the break with the USSR in the early sixties was balanced by its links to Third World countries and the Non-aligned movement: here we can mention the participation of Chou en Lai at the Bandung Conference of 1955 among another 27 nations.
2. After the dramatic change of US and Western policy towards China and its diplomatic recognition (1971), China joined the UN Security Council and had its first experiences with political multilateralism. However China kept to a merely instrumental approach to the UN, specially avoiding any commitment to UN peace missions.
3. The economic opening decided by Deng Xiao Ping from 1978 profoundly changed China's external economic relations. It was more open to the pressures of the Committee on disarmament and international economic organizations; even before the hard times following the Tiananmen crisis of 1989, the government's report to the fourth session of the 6th People's National Congress (1986) asserted that 'China would participate in various international conferences and organizations, develop positive multilateral diplomatic activities, and make efforts to enhance cooperation in all areas'.
4. The current period is characterized by a more mature combination of bilateralism, regionalism and multilateralism. After a first stage focusing on the membership of global multilateral organizations, notably the WTO, the China has been asserting in its own way multilevel multilateral cooperation both at global and regional levels, which entails a very strong role in underpinning Asian multilateralism. The 9th National People's Congress (from 1998 to 2003) supported every kind of commitment to international cooperation, whatever global or regional and both. The 16th (2002) and 17th (2007) Congresses of the Communist party statements included open commitments to multilevel multilateral cooperation: at a regional level the need of good relationship with neighbouring countries was promoted, by emphasizing that Chinese development is an opportunity for the whole of Asia (in the security, economic and environment spheres). Among the variety of forms of multilateral cooperation, the CPC has emphasised the roles of state diplomacy (strategic links with the US, France, UK, Japan, Mexico, EU and ASEAN, etc.) within the framework of the UN Charter, but also of transnational links in terms of 'folk diplomacy' and party diplomacy.

However, the nature of this regional cooperation around a peacefully emerging China is not yet clear: historians mention the old tributary system of China of pre-colonial times as a reference point. What form will the Chinese role take (leader, regional hegemon, feared great neighbour) within these new regional frameworks? Will it be of a hierarchical or multilateral nature?²¹ Second, which will be the limits and borders in terms of the call for an East Asian Community, a community desired by ASEAN and an Asia-Pacific community advocated by the Australian Prime Minister and open to the US? Third, what about the link between regional cooperation, the rule of law and democratic consolidation? The 'ASEAN charter' of 2007 announces a greater respect for human rights in the region, while the double Myanmar crisis of 2007/2009 (the uprising in the winter and tsunami in the spring of 2008) confirms the continuing strength of the traditional principle of non-interference and the idea of sovereignty as protection of a national regime (dictatorship). Fourth, international literature is increasingly looking at a new concept of 'institutionalization' of regional relations which bridges the two alternative paths of regional cooperation: the hyper-institutionalized EU method and the informal Asian way²².

Notwithstanding these significant current problems, is it realistic enough to image a long term commitment of several East-Asian states, including China, within the multitier multilateral framework? And will multilateral cooperation bring change with regard to the gradual and free self-limitation of the classical absolute understanding of national sovereignty? Will the high officials and diplomats representing the participating countries experience a kind of learning process, not only limiting transaction costs, but also sharing information and developing mutual trust within institutionalized organizations at regional and global levels (including the WTO, the UN, the International Olympic Committee, the World Health Organization, etc.)?

Several statements and practices of China, including the Party Congress resolution of 2007, mention the transition 'from multipolarism to multilateralism as a strategic option for China'.

The research should deepen this crucial subjective and discursive variable as complementary to the assessment of cooperation practices. Only to the extent that the answer to these questions is at least partially in the affirmative, could the EU type of multilateral culture be of some help within this challenging region.

On the contrary, in the case of a new imperial logic, in the case of a return to the classical balance of power logic, the EU will necessarily become even more marginal than now. Contrary to the abovementioned new multilateral scenario, several theoreticians of the alternative models of capitalism (Singapore, China, Vietnam, etc.) argue that the Asian century will not include multilateral dialogue with Europe as an essential feature, precisely because of the multipolar character of the emerging world. A second caveat is that a number of representatives of China and India argue that 'multilateralism needs multipolarism', according to the lessons of both the movement of developing countries after 1945 towards the principle of equal sovereignty of states and the relevance of unipolarism in destabilizing multilateral organizations and dividing regional entities (2001–2007). We must not forget, as asserted by Zhimin Chen, that China, by combining its interests, principles and capacities within its concept of responsible diplomacy, is often subjected to contradictory demands, not only by southern and northern partners, but also by countries in the West²³.

That is why we cannot conclude this paragraph simply by contrasting alternative concepts and approaches to multilateral cooperation in the EU and in East Asia. On the one hand the 'Asianization' of multilateral cooperation in East Asia and the centrality of China within this dynamic are a matter of fact; this makes the scenario of a 'pluralist multilateralism' realistic for the decades to come. However, on the other hand, interdependence matters more than relativism and self-isolation: the multilateral, multidimensional, multilevel, multi-actor interaction between the West and East Asia, and particularly the EU with China and East Asia, is already provoking communication, mutual recognition, cross-insemination, reciprocal understanding and adaptation, in one phrase, a process of change. The door is open to a new global and regional multilateral cooperation. What we do mean by this concept?

4. The chance for a new multilateralism

The theoretical framework for a new epoch of multilateralist studies can only be provided by combining area studies, notably, European studies, with international relations studies. On the one hand, European studies have to overcome inward looking approaches and Eurocentric understandings of reconciliation between previous enemies only through the 'community method' of supranationality; on the other hand, international relations studies should reject marginalization of the EU experience as totally irrelevant for other continents and on the global scale and learn from comparative regionalist studies. Provided these conditions are met, new multilateralism is heuristically fruitful, an important extension of government research programs, an alternative agenda in global governance studies: a modification (not an abolition) of the logic of sovereignty and maybe, the first step towards a bottom-up universalism.

In accordance with what has been said before, three features are already characterizing the new multilateralism:

5. A post-hegemonic leadership at a global level. The US still has the capacity and the will to lead a new multilateral world; however this leadership cannot be comparable with its previous hegemony. Secondly, it has to be implemented as a co-leadership where the US and the EU show the emerging powers that there is reciprocal interest in cooperation. Given the globally positive record of increasing international autonomy after 1989 and after 2001, the EU is and can in the future still be a credible leader in global change, development policy and trade regulation. More than ever in the past, the defeat of unipolarism and unilateralism provides the world with an extraordinary window of opportunity for an equal partnership between America, Europe and Asia.
6. The new multilateralism needs a new role for regionalism and interregionalism. This 'multilevel multilateralism' should include regional and interregional governance as structural features, consistent and not conflicting with the global dimension; comparative research monitoring the trend of development of regional entities from mere state-centric regimes to intergovernmental and transnational entities.

The growing importance of the regional dimension will be confronted with two challenges: on the one hand, much of the literature in favour of free trade accuses regionalism of promoting 'preferentialism' and the risk of shifting towards a fragmented 'spaghetti bowl'. On the other hand, a mainly philosophical literature sees regionalism as a route towards cosmopolitanism.

According to the European experience, a multidimensional regional cooperation (not limited to a regional preferential trade area) will have the capacity available to face both nationalism and preferentialism (as a reaction to a WTO Doha Development Round blockade). However, the true question is not to assert a useless

condemnation of the fact of regional cooperation, but rather the following one: how to multilateralize regionalism? And how to provide the global multilateral network with regional roots, strengthening its efficiency and legitimacy?

On the other hand, cosmopolitanism argues that such pessimistic assessments of regional cooperation are far from being confirmed by the EU experience and 'Kantian trends'. On the contrary, with this understanding, regionalism could also bring us to a new universalism, based on the respect of others' traditions and an understanding of shared values: some scholars call it a 'processual cosmopolitanism'²⁴.

Regionalism is interacting with interregionalism as cooperation with two regional entities or areas belonging to two different continents; interregionalism as a distinctive feature (identity-marker?) of the EU's contribution to global governance (ASEM, Barcelona process, ACP, Rio de Janeiro process, etc.). It entails an open process of dialogue and cooperation, that involves many actors, multidimensional (political dialogue matters in parallel with economic and cultural equal partnership based on respect and mutual benefit); driven by meetings at a *high level* (heads of state or government, ministers and senior officials) complemented by ministerial and working-level meetings and activities on a wide range of political, economic and cultural subjects. Interregional agreements also focus on cultural, intellectual and people-to-people contacts between Europe and the partner continent.

Finally, a controversial topic is the relationship of the EU with individual countries. To what extent is bilateralism conflicting with multilateral interregionalism? There are two forms of EU bilateralism. First, trade partnership agreements with ACP members looked at by the Commission after the failure of the Doha Round in 2006/7. Secondly, 'Strategic partnerships' with the main powers. The latter are a consequence of the rise of the EU as a political actor: with USA, Japan, Russia, Canada and, more recently, with China (2003), India (2004), Brazil (2007). When looking to the statements, these strategic partnerships entail support for regional cooperation. However, both kind of bilateralism appear to be contradictory to the EU's regional identity and are the cause of disputes. The same could be said for the bilateral trend as the Free trade agreements with individual countries are concerned.

All in all, we have no doubt that the main research findings are likely to see more regionalism and interregionalism in the 21st Century than in the 20th, even if academic research has stressed alternative routes to regional cooperation. What is needed is monitoring as to whether potential relevant pillars of a global multilevel governance are developing, and whether the competing strategies of single states (G4) and regional entities will have an impact on the still controversial reform of the global network, the UN, WTO, IMF, towards enhanced legitimacy and efficiency.

5. The risk of a closed shop and the debate on smaller multilateral groupings

By addressing the J. Bhagwati's criticism to regional cooperation and cosmopolitan studies of regionalism, we have addressed a theoretical problem which constitutes a guideline for our study on multilateral cooperation: it is the relationship between small groupings of states and universal multilateral organizations. To what extent and how does the number of members of the club matter as far as the efficiency of multilateral cooperation is concerned?

J. Caporaso provides a brilliant synthesis of what he defines as 'the logic of the *k* group': the smaller the *k* group, the easier it is to ensure cooperation, but the less multilateral the arrangement will be. The larger the *k* group, the more multilateral the cooperative arrangement might be, but the more difficult it will be to pull it off'²⁵. We have already presented a critical assessment of the normative evaluation of: 'less universal as less multilateral'. However, this approach is worthwhile, introducing the relevant topic of the advantages of smaller multilateral clubs, from a rational choice point of view. Within a smaller group, institutionalization may provide the opportunity of '*conditional co-operation*' (the strategy of co-operating on the condition that others co-operate), that is of *monitoring* the rules implementation by the others in a regular way. Also, a smaller and deeper group allows stepping away from specific *reciprocity* to *diffused reciprocity*; the *repetition game*, the lengthening of the *time frame*, the gradual construction of mutual trust and reputation. Many authors underline the positive impact of the *iteration* of the cooperation game, but, according to Michael Taylor, the number of club members matters and a small size strongly plays in favour of successful cooperation because larger groups increase the costs of monitoring²⁶.

The question as to whether ‘transaction costs’ grow for larger groups or are reduced within multilateral institutions is in general highly controversial, with a split between realists and institutionalists. By transaction costs, we mean the following canonical definition: all the costs incurred in exchange, including the costs of acquiring information, bargaining, and enforcement, as well as the opportunity cost of the time allocated to these activities²⁷. Whatever the theoretical approach, reducing transaction costs is relevant in explaining multilateralism.

However, for utilitarian, costs–benefit approaches, transaction costs are the true explanation of multilateral institutions, which are needed precisely to decrease transaction costs. Second, according to a realist view, wider multilateral arrangements are not only more various and heterogeneous but also more complex and complicated, which may raise transaction costs and increase implementation problems.

All in all, regime theory and game theory may indeed explain multilateral co–operation amongst states, being capable of providing public goods, even if conditional and on a limited basis, as its scope, scale and purposes are concerned. However, conditional cooperation and norm–setting may entail selective punishments and a trend towards bilateralism and exclusive clubs. That would be in conflict with diffuse reciprocity, indivisibility and long–term collaboration amongst states (which requires unconditional co–operation, according to Liza Martin, in Ruggie, 1983)²⁸.

We will come back to this crucial question, when applying theories of reciprocity on a regional and global scale.

6. From a ‘specific reciprocity’ to a ‘diffuse reciprocity’?

The pioneering book published by Stanley Hoffmann in 1961 emphasises the distinction between the law of the international structure, and the law of community, and classified the law of reciprocity between them²⁹. While reciprocity overcomes the bottom level of legalization of the international structure, the law of reciprocity does not address the level of common challenges of human–kind, necessarily entailing a pooling and limiting of states’ sovereignties.

Since then, everybody agrees about the link between multilateral relations and reciprocity. But what kind of reciprocity? And to what extent is the tendency towards a new multilateralism going to change the path of reciprocity? We already introduced this crucial theoretical distinction: ‘diffuse reciprocity’ is not reciprocity, but something broader and deeper. This central concept, developing institutionalism in world politics, varies according to different schools of thoughts and R.O. Keohane has illustrated in an admirable way the nuances of the extensive multidisciplinary literature.

Let us take a step back. What is meant in IR literature by reciprocity? Reciprocity is an ambiguous term, both ‘a symbol in politics’ and a ‘concept for scholars’ used by different schools of thought. Lawyers look apodictic: reciprocity is a condition theoretically attached to every legal norm of international law, which means that it is not at all opposed to state sovereignty³⁰. On the contrary, it was used for more than two centuries by treaty–making, both as far as trade and political relations are concerned. However, the question is more complex. There are several reciprocities. The one that is most linked to the rational choice theory and realistic school of thought argues that it is contingent and conditional: actors respond to cooperation with cooperation, to defection with defection, whereas political values play no role at all. According to Keohane this could also be defined as the lowest level of ‘cooperation among egoists’, compatible with international anarchy and balance of power thinking³¹.

Furthermore, more critical approaches argue that superpowers or great powers often practice ‘aggressive reciprocity’ as a strategy for opening foreign markets, notably markets of weaker partners: for example, the MFN clause is conditionally applied. In the case of ‘specific reciprocity’, actors don’t need any mutual middle term and long term trust and the game theory works as a valid general scientific framework. However, a certain degree of equivalence is needed. In the case of leonine pacts, one–sided exploitation, imperial domination or unbalanced vassalage, in summary, in the event of lack of any equivalence, the term of reciprocity is totally unfit. In this respect, J. G. Ruggie is right in emphasizing the historical break between both the German and Japanese models before 1945 of relationship with vassals, partners and allies, on the one hand, and on the other, the principle of equivalence of reciprocal concessions and benefits, typical of the multilateral institutions established by the USA after Bretton Woods (IMF, WB) and 1947 (GATT). Of course, the equivalence is only

partial and the effective power relations affect the practice of mutual concessions³².

In historical terms, specific reciprocity has contributed to international cooperation during the decades of both UK and US hegemonies. However, reciprocity has met problems both in bilateral and multilateral contexts, in trade and security negotiations. When the bilateral relationship between two superpowers is highly competitive (USA–USSR), even the concept of equivalence is a controversial one. An echoing of past conflicts mattered and did cause deadlocks.

Multilateral specific reciprocity might be even more difficult to achieve according to Keohane: where there is a large number of participants, the existence of public goods (indivisible by definition) gives rise to a temptation for ‘free riders not to pay for the good but to gain from its provision by others’, which is greater than for bilateral or small group negotiations (the risk of retaliation is lower)³³.

b) ‘Diffuse reciprocity’ is a more complex and theoretically innovative concept, linked to the literature on social exchange. According to Keohane, ‘diffuse reciprocity’ is characterized by a less strict and rougher equivalence of benefits and more consistency with general principles, as, for example, the unconditional MFN clause.

As said by Keohane, summarizing a large US literature, diffuse reciprocity is ‘an ongoing series of sequential actions which may continue indefinitely, never balancing, but continuing to entail mutual concessions, within the context of shared commitments and values’. In academic terms, it calls for a multidisciplinary approach, including not only economics but also political science, law, anthropology and sociology.

Diffuse reciprocity is more constraining and entails obligations. Social scientists are better than rational choice economists at explaining why not only individuals but also states sometimes behave on the basis of what Albert Hirschman and others call ‘solidarity’, notably between richer and poorer individuals, regions, or states, or by voluntarily contributing to the public good. Mere positivist and utilitarian approaches are challenged, while, according to Keohane, the literature on social exchange, for example Barrington Moore, Alvin Gouldner and Charles Lindblom, might frame behaviours consistent with diffuse reciprocity and the obligations which are linked to it. The problem is whether, contrary to any Hobbesian approach, obligation and gratitude matter in international relations as much as within national and local societies.

According to this literature, exchange takes place not simultaneously but sequentially, in order to underpin a long term multilateral or bilateral partnership, including obligation: debts and credits increase reciprocal trust over time, where complete repayment is not only not needed but inhibited according to Gouldner. Mutual trust is inversely proportional to the degree of application of simultaneous reciprocity, which is on the contrary usual between enemies (exchange of prisoners and spies, cold war disarmament negotiations) or trade competitors. Sequential reciprocity provides partners with information about the others’ habits and consistency with principles.

Sequential exchange may also mean, according to Caporaso, a reciprocity including various policy fields³⁴. For example, in 1990/91, Germany obtained the ‘yes’ of neighbouring France, Belgium, Netherlands, and later on Poland, to both German unity and sovereignty, by offering its beloved DM to Europe, through the new Maastricht Treaty. Issues linkage is a sensitive and controversial issue³⁵.

Institutionalization interacts with diffuse reciprocity. Regime building, as a first relevant step, includes arrangements not only regarding contents of mutual interest but also regarding the way of managing conflicts, rules and procedures and general principles of conduct. Furthermore, multilateral regimes focussing on common goods (as the Kyoto Protocol) are only justified by a diffuse reciprocity approach.

7. Deepening regional multilateralism. The EU as a model of diffuse reciprocity?

The US academic literature offers a relevant background for reciprocity studies. However, the interplay with European studies is giving the new concept of diffuse reciprocity more substance, on the basis of the EU experience and comparative studies about regional cooperation. Both comparative regionalist studies and US theoretical literature are precious because they prove that the EU experience is not an isolated case but a part of a more general tendency towards a multilateral framework where diffuse reciprocity is less rare than in the past.

Consistently with the previous presentation, we would like to deepen a European point of view, emphasising, even more than Keohane that, between bilateral reciprocity on the one hand, and, on the other hand, weak global reciprocity, a third level of strong regional arrangements may allow a top level of diffuse reciprocity. A small group of states, for example of regional partners (not only the EU but also MERCOSUR and the ASEAN) could develop several relevant complementary tools allowing a more effective reciprocity through stronger institutions and less defection than a multilateral network at global scale. A smaller group makes a better multilateral monitoring of each other's behaviour at regional scale possible, by setting more compelling and multidimensional institutional arrangements or by institutionalizing sequential exchanges.

In my interpretation, diffuse reciprocity is a broader and deeper form of reciprocity, entailing consequences for both domestic institutions and societies of participants.

E. Haas has been a true pioneer in giving support to this argument, when providing the first bridge between international relations and regional integration studies and arguing that regional regimes and organizations are the best approximation to diffuse reciprocity³⁶. Indeed, diffuse reciprocity is particularly well illustrated by the negotiation-machine represented by a regional entity such as the EU since its origins in the fifties, where multilateral reciprocity among member states has been upgraded from maintaining of sovereignty to pooling of sovereignty. Of course, since 1973, a widening Europe makes a working sequential exchange more difficult and complex. However, it would be wrong to argue that only the Jean Monnet kind of EC – with deep integration, community method, supranationality, and teleological ideology – has implemented diffuse reciprocity, whereas the EU 27 is returning to specific reciprocity and 'caws market' practices. On the contrary, in spite of this challenge, new methods of regional governance and of multilateral coordination (such as the WTO, and enhanced cooperation) are making diffuse reciprocity likely to become extended within new policy fields and realms.

Is this paving the way to the unilateral export of the 'EU model' abroad at a regional and global scale? We don't think so. Various empirical examples are provided by Mercosur, Andean Community, ASEAN, 'ASEAN plus 1', 'ASEAN plus 3', including the Chang May initiative (and plus 6), 'A.R.F', 'Six-party talks about the Korean peninsula', 'Shanghai cooperation organization', Asian Payment Network, SAARC ,among others and show a large array of cases from sovereignty pooling to sovereignty enhancing regional entities.

The thesis of the uniqueness of the EU is well founded on concrete empirical evidence. Despite its limits to 1% of the EU states' total GDP, the EU budget brings evidence of diffuse reciprocity: it shows both internal redistribution between the richest and poorest among the 27 according to the principle of regional solidarity and convergence and external solidarity with developing countries³⁷. The EU-ACP program is relatively speaking the most generous when compared with those of the US and Japan. How do we explain these facts without taking into account the values and ideas of Europeans explicitly incorporated within the institutional set established by the Treaties?

These standards of behaviour are not opposed to the self-interest of states, but go beyond it. In the European experience, starting with the ECSC of 1952 and the EC of 1957, the process of deepening and widening the common market enhanced mutual mid-term and long-term trust among the growing number of participants. It also meant that it won its competition with the 'specific reciprocity'-oriented EFTA, the European Free Trade Association, which has been in decline for several years as a consequence.

What is interesting is that, out of any state building dynamics, the integration of their internal agendas did gradually take the member states and societies beyond traditional trade relations, to an increasingly deepening convergence as far as the national evolving social models and sustainable development are concerned. This factor is crucial in explaining the EU success story and the stability of the European construction. What is interesting is that countries such as the UK and the Scandinavian countries at first rejected any diffuse reciprocity at the European level and later on opted in favour of the J. Monnet-founded EC, leaving EFTA to its inevitable decline. This proves that there is a possible evolution from specific to diffuse reciprocity, even if traces of the past merely utilitarian approach are still clearly visible.

Internal diffuse reciprocity is however comparatively stronger than the external version: comparing the EU Structural Funds (accounting for one third of the total community budget) and the ACP program brings evidence of this. On the contrary, the Scandinavian states' tradition of solidarity at a global level (by far the first donors at global level) conflicts with their scepticism about solidarity at a regional level. Seen from Brussels, the Scandinavian Euro-scepticism looks like Wohlstand-egoismus, whereas when seen from Stockholm, the Brussels approach seems to be fostering a European fortress. There is merit in both arguments. On the one hand, a new and deeper link between internal multilateralism and external multilateralism might strengthen diffuse reciprocity at the international level. On the other hand, contrary to idealistic approaches, analyzing the links between specific and diffuse reciprocity may help the behaviour of both Scandinavian states and the EU.

The external challenge of conflict-causing globalization fosters new dynamics. Several papers by the Commission and the Council, parallel to the evolving practice of external relations, do include the internal modernization agendas of the evolving social models and sustainable development (of both EU and the partners) within international multilateral and bilateral relations. What looks particularly interesting is the gradually emerging link between such an internal diffuse reciprocity and the deepening of external relations both at bilateral and multilateral levels³⁸. The EU's self-interest is evident: to avoid a race to the bottom as far as social, fiscal and environmental standards are concerned.

However, there is an interest for partners as well, for example in acquiring knowledge of the best modernization performances, importing European technologies and stabilizing their access to the richest world market by enhancing socio-environmental standards. Finally, both sides share an interest in constructing global alliances to face up to the common global challenges of poverty and climate change.

We are fully aware that the emphasis by Haas, Keohane and ourselves on the regional dimension as the best framing for diffuse reciprocity might be inconsistent with the classification of the unconditional MFN clause (automatically extended to third parties) as diffuse reciprocity³⁹. Why? Because in the free trade context not only is the EC/EU considered an exception as a customs union (Art. 24 GATT and WTO), but it is also proven that regional trade regimes provoke deviations as far as global trade is concerned. What lies behind the following apparent paradox? The main trading power and the regional regime with the highest record of diffuse reciprocity, is in conflict with unconditional free trade? which is, on the other hand, considered by many, to be an excellent indicator of diffuse reciprocity. This paradox is challenging for interdisciplinary research because the main social/political science literature openly conflicts with the finding of mainstream free trade and IPE literature opposing regional to global liberalization and non-discrimination.

Furthermore, in general, free trade studies focus on regional regimes and associations of states, such as mere preferential trade areas (PTAs), custom unions, optimal currency areas and they contrast them with global free trade and economic cooperation⁴⁰. Whatever our normative understanding, the question of trade diversions provoked by regional PTAs is a relevant one. While looking at globalization with a new realist approach, R. Gilpin shares some findings of the argument contrasting regions to globalization.

However, the idea of the existence of natural economic zones is shared by Braudel, Wallerstein, Hettne ('regionness')⁴¹. When pursuing a functionalist research strategy (Bela Belassa⁴², Haas, etc.), relevant scholars argue that, even as a 'second best option', regional arrangements do foster multilateral globalization and universal free trade. Even the USA, after decades of opposition, conceded to regionalism, by establishing NAFTA in 1994 and looking (until 2008 unsuccessfully) at a Free Trade Area of the Americas, from Alaska to Patagonia. It is a matter of fact that enhanced infra-regional trade is a crucial indicator for successful regional groupings⁴³.

In conclusion, there are two main ways towards 'diffused reciprocity'; the unconditional MFN clause and deepening regional cooperation. The first one 'exposes its practitioners to the risk of exploitation' by free riders. The second one risks downgrading towards inward-looking protectionist paths. Both need strong global institutions to limit the dangers by top-down regulation. The second one needs to expand from Europe horizontally and bottom-up, towards other regional and global networks, and consequently to evolve towards a multilevel multilateral tool of governance. As a bridging literature we mentioned R. Keohane; we could also mention L. Summers and P. Krugman, who argue that geographic proximity makes of infra-regional trade something natural, not necessarily acting against global liberalization. In his already quoted article, R. Keohane also stresses the dialectical interplay between specific and diffuse reciprocity, sometimes applied in a combined way by states.

Last but not least, constructivist approaches suggest that the way states understand their own self-interest changes according to the perception of the other's behaviour. Common institutions are the best (even if not the only) framework for mutual information, obligation, trust-making and enhancing all preconditions of diffuse reciprocity. This has happened at the WTO level from the beginning and despite the problems of both the Uruguay and Doha rounds. However, this is more likely to happen at a regional level where values, history, feeling of identity, common aims and fears, make communication easier, as regional entities such as the EC/EU well show. The cognitive dimension and the communication at an institutional level interplay with the level of civil societies and individuals.

8. Legitimizing multilateral governance

The open controversy regarding the legitimacy of the multilateral network is composed of several elements. Firstly, there is the substantial legitimacy side, based on the system efficiency. The specific benefits for the ordinary citizens are a key indicator of legitimacy both at a regional⁴⁴ and global scale. The current efficiency gap (of IMF, WTO, WB, FAO) the limits of the capacity of mastering the dark side of globalization, its imbalances and injustices, seriously affects the legitimacy of the multilateral system, notably according to the antiglobal movement and to the representatives of the third world countries.

Secondly, a well rooted school of thought pays very much attention to the legitimizing role of the epistemic community. Technocratic theories of power help by emphasizing the crucial role of knowledge by stabilizing every level of governance and enhancing the ability of organizations by providing citizens with public goods. Expertise matters, both at regional and global levels, due to enhancing the efficiency of multilateral performance, just as it used to matter during the history of nation-state building. This has been emphasized, for example, by 'mixed government' theories, including 'democracy', 'aristocracy' (technocracy) and 'monarchy', as constituent co-elements of the long-term stability of polities⁴⁵.

Thirdly, the 'input legitimacy' side, that is legitimacy by participation, is linked to the question of international democracy. It presents two main poles. On the one hand, a first approach is based on the realist theory that democracy has not very much to do with international relations, and will always be limited at the level of local and national government. According to this minimalist model, what matters is the extent and consolidation of domestic democratization. The firm distinction between democracy within the state and democracy without the states is asserted. Regarding the smaller context of the EC/EU, according to Andrew Moravcsik, the democratic deficit is a myth, because each member is a democratic state⁴⁶. Democratic states provide the Council and the European Council with indirect but solid input legitimacy through democratic support by citizens. The same could be even more valid at global multilateral level, where any similarity with a national democracy is out of question. However, it is highly significant that A. Moravcsik recently joined R. O. Keohane in addressing the question of an increased legitimacy of the multilateral network⁴⁷.

On the other hand, according to an extensive and pluralist school of thought, domestic democracy is a necessary but insufficient precondition for international democracy. No Chinese wall exists between inside and outside the state. Not only must international life be democratized in order to break one of the main external limits to domestic democracy (power politics, according to N. Bobbio⁴⁸), but the latter would be undermined if the world system is maintained at the level of quasi-anarchy and global governance as a mere technocratic business.

Moreover, what was inconceivable some centuries or even some decades ago is on the agenda of the 21st Century. Democratic aims and ideals increasingly support transnational citizens' demands for participation in the supranational decision-making process⁴⁹, and the cosmopolitan book written by E. Kant a few years after the French revolution is more appropriate than ever⁵⁰. A various and pluralist movement of global public opinion emerged during the last decade opposing multilateral organizations and democracy. It is becoming practically impossible and theoretically obsolete to imagine providing the regional and global institutions with more regulating power without enhancing standards of democratic legitimacy and accountability. According to N. Bobbio, the concept of international democracy is not only based on the democratization of the units composing the global system, but also on two more criteria: the democratization of the relationship among states and of the system itself.

The mainstream of this cosmopolitan school of thought has been for many years attracted by the utopia of a global democratic state based on regional federal states, starting with the model of the EU. The domestic analogy brings some of the authors to the perspective of the UN as a world government of globalization, eroding and transcending national sovereignties. Protection of human rights is conceived as leverage to humanitarian intervention and limits to national sovereignty. The UN system in its current state merits several criticisms: however, its democratization is linked by this school of thought with the powers of the Assembly, conceived as a kind of global parliament in the making⁵¹. The end of the veto right of a few great powers within a reformed Security Council organised according to rotating criteria is also required to enhance legitimacy through representation. Some students envisage a pyramidal construction: under this arrangement, regional federal states may give birth to a new regionalized UN system and Security Council⁵².

The problem is that the analogy with national democratic standards could be misleading and raise expectations too high: the democratic sphere, the method of appointing and scrutinizing officials, the degree and form of participation, power limitations, are qualitatively different at the national or supranational levels. The same word –democratic legitimacy– covers two distinct realms with two necessarily distinct sets of rules, procedures, public spheres, etc.

A lesser but more realistic indicator of international democratization can come from enhancing the capacity of multilateralism to support and strengthen democracy. A third school of thought rejects any opposition between multilateralism and democracy while recognizing a certain negative impact of global and regional elitist institutions on domestic democracy. It stresses three elements. First, according to D. Held and his school, multilateralism might be complementary to the insufficiencies of national democracies, by addressing the regulation of private organizations, lobbying, companies, free riders, acting at on transnational scale⁵³. In this case, however, the main issue at stake is not the democratization of multilateral institutions but their enhanced efficiency, using the power resource of pooling national sovereignties together, as a means of reducing the deficit and limits of domestic democracies. Secondly, a commitment to multilateral cooperation may amend any national feeling of superiority, internal limits of crypto-ethnocentrism, 'parochialism', and arrogance of national democracy, as shown by Keohane and Moravcsick. We add a third element: a softly constraining impact of multilateral cooperation on participant states. For example, in the case of transition countries, where democracy and the rule of law are still fragile or marginal, multilateral cooperation strengthens the role of the branch of civil society, networks and of civil servants respecting international standards, multilateral rules and procedures on an equal basis and this cannot but put a brake on and weaken nationalism, arbitrary behaviours, authoritarianism, the shadow economy, etc. We can define this third impact as sovereignty-civilizing. By pooling external sovereignties within a multilateral network, regime, organization, a state is committed to change, to some extent, the exercise of internal sovereignty, according to internationally more acceptable standards and binding criteria.

Through all these routes to enhanced democracy, the EU plays the role of an advanced workshop. Notwithstanding its increasingly clear limits as a federal blueprint of a global state, the EU institutional establishment is openly suggesting that democracy is on the agenda beyond the nation state. It is already widely recognized as the most advanced step, or at least as a relevant laboratory of supranational input legitimacy: the democratically elected European Parliament ensures representative democracy while the dialogue between social partners and the myriad of social and economic and cultural networking provide more than a minimal degree of social legitimacy. The elements of participatory democracy (the petition right, and the new right of law-proposal provided there are a certain number of transnational citizen signatures) will increase through the current treaty revision.

What is very relevant is that comparative research, including that organized by Garnet⁵⁴, shows very well that the EU is not an isolated case study: the more the politicization of regional cooperation progresses in the world, the more democratic accountability and legitimacy emerge as a logical complementary objective. Regional parliaments are in progress both in Latin America and Africa. Interregional parliamentary dialogue, established by the European Parliament, is charged with controlling and strengthening interregional partnerships. A certain degree of at least consultative interaction between regional entities and the UN system is occurring. EU supports both democratic consolidation at a domestic level and democratic control of interstate cooperation at regional and global levels.

Europe is not at all isolated in claiming for a democratization of the world polity. Beside the parliamentary forms of participation, networks of civil society groups matter as far as the decision-making process and the transnational relations are concerned. Network-based bottom-up multilateral cooperation is maturing: knowledge networks are broadening and deepening scientific and academic cooperation global policy networks, executive networks, inter-parliamentary dialogues and public policy networks are increasing the circulation of best practices and ensuring a transnational and intergovernmental learning process. Transnational advocacy networks are setting down the roots of global multilateral politics deep within civil societies of the North and South. Finally the role of migration flows (200 million in 2008) and of the diasporas in Europe, Asia and the Americas is crucial in overcoming a traditional, diplomatic, elitist, technocratic version of multilateral cooperation.

Richard Higgott has listed the deliverables of such a network: agenda – and standard– setting; improving modes of coordination and policy implementation; exchanging of resources and pooling of authorities; providing public goods and mutual knowledge and venues for policy entrepreneurship and innovation; offering a vehicle for consensus building and reducing the participatory gap.

All in all, new and better multilateral governance for the 21st Century could hardly avoid the challenge of more articulated, pluralist, multi-actor, democratic legitimacy and accountability. Of course the model and standards of a national state democracy are clearly not applicable on a regional or global scale: however, to a certain extent, various forms and levels of input legitimacy will matter more than in the past given the growing expectations of an increasingly informed public opinion. Let us try to build up a common language of international society, towards enhanced convergence; communication, dialogue and semantics matter.

9. Conclusion

A new multilateral scenario is not at all excluded by the current evolution of international relations, provided that the following conditions are implemented by international and regional institutions:

- there is a weakening of Westphalian tendencies towards unipolarism, bipolarism and a multipolar balance of power, while the states can be seen as a political resource for multilateral cooperation;
- multilaterally, there is a counteracting of the trend towards bilateral and regional fragmentation at different levels; –? a new multilateralism needs the complementarities between regional and global dimensions of multilevel multilateral cooperation to be enhanced;
- multilateral commitments are provided with more efficiency and consistent implementation: efficiency also means enhanced coordination among multilateral institutions dealing with the same issue and monitoring systems for follow-up;
- legitimacy means not only efficiency, but also more transparency and democratic accountability, both at a national and supranational level. Legitimacy is a central challenge for the 21st Century–On the one hand, multilateral cooperation might strengthen national democracy, on the other hand, it can be influenced and politicized by the pressures of civil society, and NGOs, networks and the private sector must be part of a new era of multilateral, pluralist, multi-actor cooperation providing public opinion with a critical role stimulating efficiency and consistency with the asserted values.

All in all, multilateralism could be upgraded step-by-step from an historical instrument of a Westphalian order (whether unipolar, bipolar or multipolar) towards a political system of global governance, according to the following definition: *New Multilateralism is a form of multilevel collective transnational action and co-operation amongst states and civil societies, regarding global governance and world politics. It implies generalized principles of conduct and diffuse reciprocity, and includes several degrees and types of institutionalization, from arrangements and regimes to established organizations? The institutionalization process is expected to increase legitimacy and efficiency.*

Deepening and strengthening more binding and legitimate multilateral institutions, regimes and arrangements, entrusted with addressing the common challenges of humankind (and not merely as an instrument of a power or of an alliance or of a regional power set against other powers or alliances or threats⁵⁵) is the most powerful and farsighted political idea, born in the 20th Century at a regional level and which will eventually be on the global agenda of the 21st Century.

10. Endnotes

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- 37 Which however amounts in 2007 to more than 13000 Million Euros, 1% of the total GDP of the EU–27, out of 13000 Billion Euros, superior to that of the US.
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Chapter 2

Soft diplomacy in EU – China relations

Juliet Lodge and Angela Carpenter

1. Introduction: Multilateralism in context

The concept of multilateralism can mean different things. It embodies several underlying assumptions about the nature of relations between two or more actors and their strategic intentions. In practice, it is synonymous with complexity. Multilateralism is a tool for organising complexity and making it amenable to negotiation in multilateral settings, by working towards a single negotiating text and goal. A number of theories have been developed to explain the internal dynamics of multilateral negotiations. These range from different international and integration theories to negotiation analysis, cultural dynamics, systems theory, decision theory, game theory, coalition theory, organisation theory, network theories, agency and agenda setting, globalisation and new institutionalism, and so on. This multiplicity of theoretical approaches illustrates how diverse multilateral negotiation in practice relies on dynamic pluralised inputs and how different approaches identify the interplay between strategies and functionally linked management, brokerage, distribution, sharing and exercise of power.

2. Why Multilateralism?

Multilateralism refers to negotiations and relations based on one-to-many states rather than one-to-one state interaction. Multilateralism is designed to produce mutually beneficial outcomes. In the case of relations between China and the EU, the EU committed itself to a strategy of comprehensive engagement in April 1998¹ and this has an internal and external dimension for the EU. Internally, EU member states, through their institutions and internal processes and practices of collaboration and integration, try and overcome or reconcile any differences, rivalries or disagreements they may have regarding all manner of relations with China. The advantage of this is that it allows them externally to develop a common position among themselves that can be presented to China. This benefits China because it means that China does not have to repeat negotiations with every EU member state. Instead, it can explore how each of the EU 27 goes about implementing commonly agreed goals –for example on boosting green industry– and see how this matches best with its own priorities in international multilateral negotiations.

For the EU27, multilateral negotiation and multilateral international diplomacy inevitably means that member states have to negotiate internally to reconcile their own positions. They try to create unity between negotiation at the actual and symbolic levels which means that, despite differences of opinion and disagreement, there is always a high probability of convergence and agreement. Generally, the EU seeks to apply the same principle of high commitment to achieving a constructive outcome in its international multilateral diplomacy. This is one of the reasons why the EU's new External Action Service is expected to reduce complexity and engineer greater consensus and uniformity in the presentation of the EU's position to third states and organisations².

This is seen as desirable for three key reasons. First, multilateral negotiations are seen as a means of building coalitions around common interests, promoting mutual understanding and resolving differences, not escalating them. Second, international multilateral negotiations are viewed as a tool to contribute to global order. Third,

international multilateral negotiations allow participants to structure interaction, procedures and systems for managing both mundane and routine issues, learn from that experience, and institutionalise constructive interaction. This has the potential to lead to productive relations that can be sustained over the longer term and to channel disagreements over sensitive issues or crises through processes designed to lead to constructive outcomes: it is about keeping channels of communication open.

A strong organisational basis for international multilateral negotiation helps to ensure that existing, unproductive antagonisms do not derail progress even if they appear to be sharper within the relatively protected confines of the multilateral negotiations. In short, multilateral negotiations provide a framework for pursuing common interests and insulating them, where possible, from deeper, problematic conflicts among the parties and in the wider international environment. This has been illustrated many times in GATT negotiations and within the EU³. Success is not guaranteed, nor can it be predicted. However, a constructive approach to resolving disputes is in-built to a greater or lesser degree: a greater degree in the case of integrated organisations like the EU, a lesser degree in the case of GATT. International multilateral negotiation provides an interface for structures, procedures, cultures and negotiation processes to be used to build consensus through group processes, coalition building, mediation and informal collaboration with associated institutions (like the European Parliament, in the EU's case) and adopting different leadership styles imaginatively to capitalise on the plurality of actors and stakeholders involved in different issues. This means that successful outcomes neither need nor respond to a powerful hegemony but depend upon high commitment to achieving shared goals.

Multilateralism is a process involving action at different levels in separate domains by two or more actors who have an interest in achieving a common goal but whose positions are so different as to make achieving that sensitive and difficult. Multilateralism allows them to pursue improved relations without losing face by operating in these different domains. Multilateralism is a term that also describes cooperative tactical behaviour by states with shared interests and goals in wider international organisations: multilateral diplomacy allows them to try and benefit from their combined strength vis-à-vis others. When applied to trade negotiations, multilateralism is associated with trade relations between states, especially state-to-international organisation relations during a transition phase from moving from bilateral state-to-state relations to a more comprehensive relationship based on common criteria. The reasons for doing so often related to the way in which multilateralism would simplify relations by developing a set of common criteria for a deepening relationship. Typically, this is associated with promoting closer political links between sometimes formerly hostile governments to facilitate discussion in less charged arena, even at times of disagreement and conflict.

A major benefit of multilateralism is that it permits all manner of relations to develop to mutual benefit at many different levels. Multilateralism allows for the emergence of relations between and among states in non-threatening, positive ways. Multilateralism in these senses relies on the tools of soft diplomacy. Soft diplomacy is about taking steps informally and sometimes less visibly to foster mutual understanding. It often implies seeking means and policy areas which are less politically sensitive, or which can be rendered technocratic, in order to achieve a goal that is politically problematic. It can mean that normal routes of securing agreement to a policy step in the domestic arena are side-stepped in order to allow especially vital matters to proceed while minimising the scope for domestic opposition. Soft diplomacy is especially useful when deep mutual antagonism between states exists or when there are such sensitive matters that must be addressed and it is important to have alternative doors open to allow talks to continue should they falter, stall, fail or become deadlocked on the core goal at the higher levels of government. Soft diplomacy therefore creates an environment where other actors, including the private sector and NGOs, can become involved to support a general government goal of improving mutual relations. The advantage is that such exchanges can be initiated and grow independently of government intervention and direction: thus, for example, sport, cultural, and educational exchanges and links can take place and be led by the sporting bodies themselves. This makes them less dependent on government-to-government diplomacy. Soft diplomacy offers greater scope for development and initiatives and allows the partners themselves to improve mutual understanding in creative and innovative ways that extend beyond the usual diplomatic elites to commercial partners and other actors. This can be especially useful to governments wishing to focus on high diplomacy issues, such as international relations, foreign policy and human rights (see Mattlin (2010)⁴, Freeman and Geeraerts (2011)⁵). For example, the issue of human rights represents a highly sensitive trip-switch in EU-China relations. Following visits to China by Baroness Catherine Ashton, Vice President of the European Commission and High Representative of the European Union for Foreign Affairs and Security Policy, together with Herman Van Rompuy, President of the European Council, in the summer

of 2011, the EU's Ambassador to China stated that a more nuanced understanding was emerging in the EU of China's approach to human rights. This does not disguise continuing divergence and tension between the two over human rights in the context of international crises and domestic Chinese practices, and the way in which it surfaces in negotiations over trade, finance, energy, investment, telecommunications, climate change and structural change in the world economy. But it does deter generalised stagnation or regression and legitimise discussion over trickier accommodation and slower change in this arena. It also shows how the EU's domestic multilateralism itself has to be better honed to achieve a common voice in order to make sense to China.

Multilateralism has two dimensions: a vertical one and a horizontal one. The vertical dimension rests on the tools of soft diplomacy to create the basis for preparing, creating and sustaining mutual understanding and sound relations across varied aspects of modern activity, often separate from and independent of government intervention, direction and control. The horizontal dimension rests on exploiting the capacity building of the vertical dimensions in order to help develop and sustain strong state-to-state relations managed by governments. Reciprocal interaction is essential to allow mutual accommodation of interests in shaping the new world economic order⁶.

Multilateralism has over the years provided a framework for comparing and overcoming different rules and regulations that disadvantage or benefit certain members over others, within the EU and GATT for example. The aim is to create common ground and equal opportunities based on accepted principles of fairness. While efforts may fall short of the objective, the attempt is made to reconcile differences in constructive ways. At the same time, it must be recognised that multilateralism can be problematic if third parties seek to undermine multilateral arrangements. For example, states can try and gain competitive advantage vis-à-vis the EU's member states by attempting to negotiate bilateral agreements with each member and setting each member state against the other in order to strike a hard bargain. This is one of the reasons why the EU's founding treaties gave competence for specific areas of 'external relations' (that is trade and commerce) to the EU Commission and reserved foreign policy to the foreign offices of the member states⁷. However, trade and commerce are no longer seen as soft diplomacy but are recognised as part of the strategy of states' international and foreign policies. That is not to say that trade and commerce are managed by governments in the EU but governments may support activities that assist in promoting trade and commerce which is so important to ensuring a state's prosperity and economic wellbeing. Moreover, governments have a stake in ensuring that the diplomatic environment is conducive to allowing independent trade and commercial relations to flourish. Within the context of the EU, the member states' governments independently and together have a keen interest in trade and commerce with states around the world. China is an especially important partner given its high penetration of European import markets.

In addition to the trade and commerce agreements mentioned above, both the EU and its member states have in place various programmes designed to help bodies develop relationships based on mutual interest between themselves and China. For example, in 2009–10, the UK Sustainable Development Dialogues Programme led by DEFRA⁸ resulted in the UK cities of Glasgow and Sheffield working with Nanjing and Wuhan to exchange experiences on urban regeneration and affordable housing. Mutually beneficial lessons were shared about improving transport planning, integrating it with land-use and promoting development through public sector investment⁹. As will be shown below, these are crucial elements in realising wider green energy and economic goals. First, however, an example of a new EU policy area –sport– is presented as one which offers scope for developing future soft diplomacy interaction because of its relative newness and consequent openness to initiatives and influence. Sport is just one policy area that can be linked to the strategic agenda in EU–China relations. Following this brief overview, this chapter will examine other examples of multilateralism in a number of strategic areas of China–EU relations– the areas of energy, climate change, marine transport and the marine environment.

3. Multilateralism and EU soft diplomacy: the example of sport

Sport is seen as a tool of diplomacy that readily transcends linguistic and cultural divisions and that helps to cut poverty and foster development. The EU Commission supports this position and joined with FIFA to promote football as a means of boosting the development of the African, Caribbean and Pacific (ACP) countries. Its 2007 White Paper on Sport introduced a more general use of sport as a tool in the EU development policy. In May 2010, the International Olympic Committee opened the first joint forum between the IOC and the United Nations (UN). At it, the importance of partnership was discussed by sporting officials and UN representatives

in order to leverage the IOC's recently obtained UN observer status and strengthen cooperation in the field of development through sport¹⁰.

The Lisbon Treaty came into force on 1 December 2010¹¹. Article 165 provides the EU with a competence for sport. It opens the door to new areas of multilateral cooperation by granting the EU Commission with a formal competence for aspects of sport. The first step was to launch a wide stakeholder consultation to prepare a sports programme due in 2012. This was based on informal intra-EU multilateralism among EU sports ministers who discussed issues raised in the 2004 'Rolling Agenda for Sport'. These covered doping, education, health and volunteering in the sport sector. In addition, and significantly, the economic and social functions of sport were considered. Gender and disability also feature in subsequent discussions and informed the EU Commission's 2007 White Paper on Sport¹² and the implementation of 53 measures outlined in the 'Pierre de Coubertin' Action Plan¹³.

These included recommendations on sport in the Union's external relations, promoting the use of sport as a tool in the EU's development policy, including sport-related issues in policy dialogue and cooperation with partner countries, promoting sport as an element in the EU's public diplomacy and when implementing the 2007 Communication¹⁴. on circular migration and mobility partnerships with third countries, and harmonised schemes for the admission of various categories of third country nationals for economic purposes on the basis of the 2005 Policy Plan on Legal Migration¹⁵. In short, sport is a soft tool of diplomacy designed to ease progress on some of the trickier and more sensitive policies where EU-Chinese positions differ. These include migration, combating international fraud and crime, international cooperation among police, customs, migration, border and law enforcement agencies. International sporting events or bilateral events inevitably involve these agencies but disagreements can be negotiated out of the limelight when sport is the focus.

Sporting cooperation and competition can be fostered on a village to village, region to region basis or national team to national team basis. Such low level links are vital building bricks in creating capacity for high level sustainable relations among states. This is because they can be developed to help address problems of modern society, including some tricky domestic issues like media censorship, internet policies, delinquency, gender discrimination, disability and human rights and health. Indeed, sport policy covers all these areas and allows states to discuss them more indirectly and in ways that help to save the face or be less embarrassing to the state whose values seem at odds with those espoused internationally. For example, discussing problems of international sport event management allows the EU and China to build understanding of the economic impact and potential of sport for realising wider socioeconomic and political objectives such as fostering political dialogue by combating discrimination based on nationality in all sports. Multilateral discussions on sport can help to establish minimum standards and exchange of best practices, and assist in promoting cooperation in other sensitive fields such as those involved in identifying and combating money-laundering and other financial crimes and corruption in the sports sector. It is interesting that the EU uses multilateral strategies internally also and starting with football organised a conference with UEFA (Union of European Football Associations), EPFL (École Fédérale de Lausanne), Fifpro (World Players Union for football), national associations and national leagues on existing licensing systems and best practices in this field. The EU has to reach accord itself if it is to be effective in negotiating with China and has consciously developed its own sports policy as a tool accordingly.

Engagement in international sports competitions is an important signal and a sign of a state's recognition on the world stage. While the EU is not a state, it does have EU teams in some areas of sport that foster multilateral relations among the EU's member themselves, such as in yachting for example. This mirrors other intra-EU cultural multilateralism such as the EU's Youth orchestra which brings musicians from different EU states together to form an EU orchestra as an expression of EU understanding both within the individual member states and on the international stage.

The promotion of greater European visibility at sporting events is important to the EU which provides financial support to two events. Firstly, the Mediterranean Games, held every four years under the auspices of the International Olympic Committee, mainly for nations bordering the Mediterranean Sea, where Europe, Africa and Asia meet. Secondly, there is the European Youth Olympic Festival (EYOF). In July 2009, 6,000 sports people participated¹⁶ in this event which takes place every two years for young athletes from the 49 member countries of the association of European Olympic Committees. The 10th EYOF took place in Tampere, Finland in July 2009¹⁷. 3,500 team members participated in the event. The EU contribution to the financing of the event was 1.5 million.

Sport is therefore an important part of soft diplomacy and a key element of multilateral diplomacy involving a plurality of horizontal and vertical actors cutting across many policy dimensions from education and culture to environmental policy, competition law, the media, internal market and external relations in general. It is a means of increasing the EU's ability to speak with a single voice in international bodies and vis-à-vis third countries. It also means that EU sports ministers now meet in official EU meetings. This does not mean that there is a heavy governmental direction, rather that the plurality of actors and sporting, voluntary, educational and social associations is recognised and encouraged. At the same time, the EU Commission sees it as a means of illustrating externally and promoting internally European values, and encouraging cooperation with international organisations and third countries. Clearly, multilateral interaction at the horizontal and vertical levels and international multilateral diplomacy in this soft area of policy has led to progress in respect of several core shared policy goals. The International Olympic Committee and its partners underline the advantages of using sport to implement actions around the world concerning humanitarian assistance, peace-building, education, gender equality, combating HIV/AIDS, and protecting the environment and realising the UN's Millennium Goals.

Sport is likely to grow as a tool for soothing more difficult relations between actors in the EU and China, notably in respect of telecommunications and especially trade, commerce and investment (covered elsewhere in this book) and the environment.

4. EU-China multilateralism in the areas of energy security and climate change

The idea of the EU and China working together was designed to improve relations between the two parties, particularly in light of the ever-closer trading partnership between the two and increasing investment by European companies into China and increasing foreign direct investment by China into the EU. The EU is now China's largest trading partner and China is becoming the EU's first source of imports for goods and also its first source of foreign trade deficit: 131 billion euro in 2006¹⁸ increasing to 160 billion euro just one year later¹⁹. Relations between the EU and the People's Republic of China began in 1975 with the establishment of diplomatic relations, and a trade agreement in 1978. A Trade and Cooperation Agreement in 1985 led to the EEC and China granting each other most-favoured nation status. The relationship has evolved from a system of one-to-one state bilateral relationships to cooperation based on multilateral negotiation. In 1994 and 2002 the Agreement was supplemented by exchanges of letters establishing a broader political dialogue. Now there are institutionalised annual summits and other high-level meetings held alternately in China and Europe. In October 2006 the EU Commission published a communication "EU-China: Closer Partners, Growing Responsibilities"²⁰ setting out the EU's aspirations for the relationship. In 2007, negotiations began on a Partnership and Cooperation Agreement (PCA) to replace the 1985 Agreement. A High Level Economic and Trade Dialogue Mechanism (HLM) was launched in April 2008 to enhance cooperation on trade and economic issues, with the participation of eight Commissioners and 10 Chinese ministers²¹. The EU and China engage in regular trade, political and economic dialogue meetings, and have over 24 sectoral dialogues that span issues of mutual interest including highly problematic aspects of environmental protection, industrial policy, space, agriculture, satellite systems, civil aviation, information society, transport, sanitary and phytosanitary issues, education and culture²².

As multilateral negotiations proceed among a range of players at different levels, multilateralism is reflected in diverse level EU-China meetings ranging from the Annual EU-China summits of Prime Ministers, to meetings of Foreign ministers, meetings between Political Directors and Geographic Directors, and meetings at expert level. They will continue as the EU new External Action Service develops. Government level meetings also cover high diplomacy issues such as foreign policy, illegal migration and human rights²³.

A High Level Economic and Trade Dialogue was set up in 2007 and high level exchanges –known as 'dialogues'– take place on exchange rate issues and macro economic matters. Divisions between China and the EU are exacerbated by mutual competition for energy, raw materials and resources²⁴. Different practices in developing market share and associated differences over quality issues regulating commodities and exports can cause tension and friction that is sufficiently strong to damage sometimes fragile developing mutual links at the higher political levels. The sectoral dialogues are especially important when conflicts arise, as for example, occurred in

2010 over the Chinese regulatory environment for foreign companies and differences over intellectual property rights, their regulation and appropriate legislative mechanisms and enforcement²⁵. These are areas where multilateral diplomacy would offer plenty of scope for going beyond the initial and necessary exploration of positions and interests to trying to elaborate common understandings and processes that would support the enforcement of commonly agreed legislative codes and regulations. For example, intellectual property rights and the associated issues of counterfeiting are sensitive issues in EU–China relations. The EU Commission’s annual report on customs detentions suggested that China is the main source of fake goods entering the EU27, even allowing for a reduction owing to the recession²⁶.

In 2003 an EU Commission Policy Paper²⁷ noted that the EU and China had ‘an ever–greater interest to work together as strategic partners to safeguard and promote sustainable development, peace and stability’. Since 1998, the EU’s main aims vis–a–vis China have been to:

- engage China through upgraded political dialogue
- support China’s transition to an open society (including respect for human rights)
- integrate China into the world economy through economic and social reform–within the context of Sustainable Development
- make better use of existing European resources and
- raise the EU’s profile in China.

China has recognised its diverse interests with the EU, but also warned the EU against interfering in its domestic affairs²⁸. In a speech by Chinese Premier Wen Jiabao to the eleventh EU–China Summit in Prague, May 2009, Premier Wen stated that ‘In conducting strategic cooperation between China and the EU, the most important thing is to stick to the principles of mutual respect and not interfere with each other’s internal affairs’. The most tense area remains deep differences between the EU and China in respect of human rights and what the EU regards as their breach in China. Growing turbulence in the EU during the recession regarding the ambivalent regulatory environment in China and differential application of rules for firms is likely to make for continuing problems and tension. Beyond that, two areas of concern and interest to both the EU and China are energy security and climate change, both of which are flashpoints as well as areas where tension can be defused to mutual advantage through comprehensive soft tools of multilateral diplomacy. It is important to remember that for all the EU member states, in international relations the EU multiplies their individual and collective interests and that at times the image of division conceals this deeply entrenched interest in common outcomes.

4.1. Energy Security

A dialogue on energy and the environment began in 1994. Since 2004, a joint Energy Development Programme has resulted in action plans on clean coal, energy and renewable resources, with the EU also committing itself to aim for zero emissions. Energy security and access to energy markets are areas of high common concern to the EU and China. The burning of fossil fuels such as coal and oil for energy generation, transport and other activities are major sources of CO₂ and other greenhouse gases (GHGs) which directly threaten the environment. This is an area which is problematic to the EU, and its member states, where targets to reduce such emissions may be impacted on by the current recession and the impacts of green taxes and the green agenda on areas such as unemployment and energy costs.

In 2006 the EU Commission set out EU policy towards China in a Communication which recognised that China is the world’s second largest, and growing, raw materials and energy consumer²⁹. The Commission noted that as Chinese prosperity increases, China has sought to find its place in the world ‘commensurate with its political and economic power’, so the EU has to respond effectively ‘to tackle the key challenges facing Europe today—including climate change, employment, migration and security’. The EU has also recognised its heavy dependence on imported gas from Russia and the Persian Gulf and the possibility of competition between China and the EU for oil from those regions³⁰.

China has plentiful coal reserves, particularly in the north and coal–based [electricity] generation remains China’s primary source of energy³¹. According to the 2009 International Energy Agency (IEA) report, production of hard coal as a percentage of global production rose from 18.7% in 1973 (approximately 42 million tonnes) to 47.4% in 2008 (approximately 2,770 tonnes)³². The IEA report noted that China consumed 7.9% of global production

of all fuels (which includes coal, oil, gas, geothermal, solar, wind and others) in 1973 (approximately 369 million tonnes of oil equivalent) increasing to 15.2% (approximately 1,259 Million tonnes of oil equivalent) in 2007. Despite its huge coal reserves, China is becoming increasingly dependent on imported crude oil and fuel oil in order to maintain its own energy security, in addition to its domestic coal reserves. The increase in consumption of both coal and oil is expected to boost competition with other countries for oil in particular, while also having significant climate change impacts as a result of China's continued growth and economic prosperity.

The EU is very sensitive to changes in the world markets for oil, food and raw materials, where significant changes in costs can affect the EU's economic security³³. China's exports of goods and services make up 39.7% of its GDP. Among its major exports are: office machines, data processing and telecommunications equipment, electrical machinery and textiles. China imports mainly commodities: iron and steel, oil and mineral fuels; machinery and equipment, plastics, optical and medical equipment and organic chemicals³⁴. To add value to these commodities, energy is essential, and therefore China, along with other states, has a keen interest in the security of its energy supplies. It has invested heavily overseas accordingly. There are very strong economic links between the EU and China and friction over trade is long-standing³⁵. Since 2004 China has become the EU's second biggest trading partner with EU-China trade almost doubling between 2000 and 2004 and with EU exports to China growing from 25.8 billion to 48 billion while imports from China grew from 74.4 billion to 126.7 billion. Growth has continued and, by 2007, EU exports to China had reached 72 billion worth of goods while imports from China had grown to 232 billion worth of goods³⁶. As a result of these strong links and on the growing dependence of both the EU and China on imported oil in particular, any lack of cooperation between the two in the area of energy may have severe impacts for the energy security of both parties³⁷. In this area it is vital that strong cooperation is maintained and activities such as EU support of the development of clean coal technology in China could be vital to potentially reduce competition for declining oil resources. Moreover, Chinese interest in the EU's ACP partners' raw materials is another area where friction is possible and where the need for astute multilateral diplomacy is growing. Congo's Finance Minister Matata Ponyo visited China in July 2010 to discuss energy and infrastructure deals, following the cancellation of debt worth \$8 billion by multilateral institutions including the World Bank that same month³⁸. Also related to that visit, Exim Bank of China promised to finance major infrastructure, including electricity and water supplies in Congo and China became the majority stakeholder in a joint mining venture with Congolese miners for copper, coltan and cassiterite needed by high tech industry³⁹. From this it appears that China continues its traditional approach towards natural resource rich countries. China's opening up to the international world, and its rapid development, make it a formidable competitor for scarce natural resources needed to fuel development and exports, and this competition also carries over into the area of energy security that is vital to both the EU and China.

4.2. Environment and Climate Change Policy

Strong cooperation between the EU and China could also be very important regarding action on climate change. Climate change refers to periods of time where a rise or fall in global temperatures have led, for example, to changes in natural weather patterns such as an increasing incidence of typhoons and hurricanes, sea level changes, and more frequent drought in sub-Saharan Africa. As the UK Meteorological Office has noted, while the Earth's climate has changed many times in response to natural causes, scientists now consider that since the early 1990s the world's climate has changed rapidly due to man made changes to the atmosphere, oceans and the land⁴⁰. The impact of climate change on maritime trade between the EU and China will be examined in section 5. This section, however, looks at the relationships and negotiations between the two parties in the area of climate change policy and the mitigation of environmental impacts of greenhouse gas GHG.

The risk of environmental damage resulting from climate change is seen by both the EU and China as a matter of global concern, despite the failure of the 2009 Copenhagen Climate Change Summit to reach agreement on a successor to the 1997 Kyoto Protocol⁴¹. The Kyoto Protocol is the international agreement linked to the United Nations Framework Convention on Climate Change and is due to end in 2012. The EU and China's targets and methods often differ in the area of climate change with China adopting 'aggressive policy goals ... to become a leader in tackling GHG emissions ... driven by domestic concerns and formulated with regard to China's own context'⁴². One of the highest environmental costs of Chinese economic development has been air, water and land pollution. While China produces fairly low levels of CO₂, it produces very large amounts of GHGs in relation to its outputs spawned by rapid growth in export industries (particularly electronics) which accounted for one third of China's emissions in 2005.

In its National Climate Change Programme (2007), China indicated that in 1994 its total GHG emissions were 4,060 million tonnes CO₂ equivalent, increasing to around 6,100 million tonnes CO₂ equivalent by 2004⁴³. It identified the dominance of coal as an energy source (69.8% of China's primary energy consumption in 2005) and the lack of modern technologies as significant challenges for China to reduce its GHG emissions in the future. On 4 March 2005, the European Commission's Directorate General for Transport and Energy (TREN) and the Chinese Ministry for Science and Technology (MOST) signed an Action Plan on Clean Coal and terms of reference for an Action Plan on Industrial Cooperation on Energy Efficiency and Renewable Energies⁴⁴. This was the basis of further cooperation in respect of energy security and research where researchers from Europe were able to gain experience of future nuclear energy use at the sites of newer Chinese reactors⁴⁵. Moreover, China wants its own nuclear industry to export and build nuclear reactors in partnership with firms outside China.

China is the world's second largest energy consumer. Its authorities revised, in the 2005 Action Plan on Clean Coal, the 2020 target to meet rising demand for clean energy, and China further agreed to cut its GHG emissions by 2020 (based on its 2005 emissions) at the Cancun Climate Summit in December 2010. 28 more nuclear reactors are to be built and its nuclear capacity is expected to make China the world leader in terms of technology and forward planning. This would increase competition for Korea and others⁴⁶ and the President of the China National Nuclear Corporation, Sun Qin, has promised a break big through in expansion overseas⁴⁷. This complements China's investment in other areas such as biotech research institutes, partnerships with foreign pharmaceutical companies in building R&D laboratories, and the growth of contract research industries in Beijing and Shanghai⁴⁸. In addition, China is likely to overtake India for IT out-sourcing and off-shoring (off-shoring being the practice of relocating work and jobs to countries with lower labour costs). While the EU and China continue to have different approaches regarding ethical issues in biotechnology, medical science and genetic engineering, it is clear that China is building capacity rapidly to address a number of core issues central to global climate change. All are strategically crucial to realising green goals.

Climate change, global warming and GHG emissions are vital to both the EU and China⁴⁹. This was stressed at the 12th EU China summit in 2009⁵⁰. China welcomed the EU Commission's provision of up to 57 million euros for a joint near-zero emissions coal (NZEC) project⁵¹. In light of the failure to reach agreement at Copenhagen, *China Daily* reported that the EU and China had established a ministerial level dialogue mechanism on climate change, in advance of the Climate Change Summit held in Cancun in December 2010⁵². *China Daily* also reported on the setting up of a climate change mechanism between the EU and China and included a statement by Günther H. Oettinger, EU Commissioner for Energy, who noted that though China and the EU 'have close contacts, ... we are at the beginning of a real partnership'. Maintaining a high level dialogue and strong cooperation on the issue of climate change may have a significant future role in negotiations on the successor to the Kyoto Agreement. Multilateralism has facilitated strong trade and economic links between the EU and China, and potentially enables spill-over to multilateral actions by them on climate change. This would allow them to exert significant influence and hopefully encourage a more successful outcome than that achieved at the 2009 Copenhagen Summit. As noted previously, the EU-China ministerial level dialogue mechanism on Climate Change was intended to arrive at a much more positive outcome at Cancun and, at that Summit, China agreed to a 45% reduction in GHG emissions against a base level of emissions in 2005, by 2020.

In view of increasing trade between the EU and China, and the strong influence China holds over world markets for oil, food and raw materials, multilateral agreement on areas such as energy and the environment are vital. Exploiting bilateral relations without tending multilateral gains could engender mutually detrimental conflict. For example, the EU and United States accused China of restricting the export of key raw materials used in the production of steel and other industrial products in a complaint filed in July with the World Trade Organisation⁵³. Keeping the door open by using the tools of soft diplomacy is crucial. Trade-offs are possible for both parties. It has been suggested that in return for receiving technology transfers on energy efficient and renewable technologies from the EU, China should set specific domestic targets on emissions post 2012 and also 'commit to the accelerated development of clean coal ... and carbon capture and storage technologies'⁵⁴. China's primary goal is to ensure that the EU's position on climate change supports rather than hinders [its] economic development. It has sought EU funding for Chinese regions likely to be 'hardest hit by climate change'⁵⁵. Among EU member states, France has a particular interest in the development potential of the nuclear industry and seeks greater engagement on that issue in China, as does Russia⁵⁶. In April 2009, China and France renewed their agreement on cooperation in the peaceful use of nuclear energy. The first Franco-Chinese protocol was signed in 1982. The three year protocol, the tenth of its kind, includes efforts in radioactive waste

treatment, controllable nuclear fusion and personnel training. In November 2009, China Guangdong Nuclear Power Group and Areva of France signed an eight-billion-euro nuclear energy deal, the biggest commercial contract ever signed by France's nuclear energy industry. The two sides will work together to establish two European pressurized water reactors at Taishan in Guangdong⁵⁷.

In July 2010, the 35th anniversary of the setting up of relations between the EU and China, the productive result and potential of multilateral diplomacy in the chronically difficult field of climate change was illustrated following a meeting of the EU–China Civil Society Round Table in Chongqing. Subsequently a seminar on Trade and Development took place in Shanghai from 22 to 24 July 2010 and this showed the way in which multilateralism at horizontal sectoral and vertical levels provides opportunities to continue crucial dialogues in different yet related forums. The seminar was linked to EU Trade Days and focused on: Trade and Development, Trade and Climate Change; and Investment and Cooperation. It was attended by representatives from non-state actors, academics and public authorities who agreed on the need for further cooperation to combat climate change and using trade as an instrument to promote green growth, trade in environmental goods and services— notably wind and hydroelectric turbines, solar-powered boilers, solar panels, seawater desalination plants and waste water reuse and treatment. The potential for extending multilateral cooperation within other multilateral organisations was exemplified by the EU and China indicating a need to cooperate in order to deal with issues hindering agreement on lower tariff barriers in the context of World Trade Organisation deliberations, focusing on reducing obstacles to investment and non tariff barriers which continue to seriously hamper the spread of environmentally friendly products⁵⁸.

At the Shanghai World Expo in July 2010, the EU and China clearly linked climate change, trade and green energy and the projects presented illustrated again how multilateral action at different levels is helping to forge deeper cooperation. On 5 July, at the *EU–China Smart City Forum*, Günther H. Oettinger, EU Commissioner for Energy, delivered a keynote speech on ‘The EU and China: working together for better cities and for better lives’ referring to the overall theme of the World Expo 2010⁵⁹. China announced that it would host an extra round of negotiations in Yianjin in October 2010 designed to promote agreement over a new climate treaty before the next ministerial meeting in Cancun, Mexico from 29 November to 10 December 2010. Achim Steiner, UN under-secretary general and director of the UN Environment Programme (UNEP) told the *China Daily* that the aim was to introduce new ideas to lead to a binding treaty which officials expect to be concluded at the end of 2011. China's position on the control of emissions is seen to be critical especially after the fraught negotiations in Copenhagen. EU Climate Action Commissioner Hedegaard stated, after a meeting of the Major Economies Forum on energy and climate in Rome on 1 July 2010, that discussions were proceeding multilaterally to ‘see if some kind of messages ... can be channelled into the formal negotiations, for instance on MRV (monitoring, reporting and verification)’⁶⁰. Progress on MRV is seen to be the key to getting agreement. Against this, there is growing criticism of carbon-offsetting practices which benefit EU competitors, such as India and China. In July 2010 an NGO Sandbag report presented data on how European industries subsidise direct competitors in Chinese and Indian steel by buying international credits to offset their carbon dioxide emissions. Under the Kyoto Protocol, industrialised countries are able to use this practice (the Clean Development Mechanism, CDM) as a way of partly meeting their climate targets by investing in carbon reduction projects in developing countries. This is designed to function in a way that shows that the CO₂ emissions could not have been secured without foreign investment. The system is open to abuse and urgent reform is vital⁶¹.

These examples illustrate the constructive and productive outcome of a process of multilateral negotiation and exchange that has enabled EU-Chinese relations to develop at all levels even though some very tough, intractable and difficult problems remain both in respect of that drawing the highest criticism –human rights in China– and those where interests clash on matters of trade, intellectual property, dumping⁶², global warming and economic prosperity.

5. Climate Change and Maritime Trade

Maritime trade is vital to both China and the EU and for China. Trade with the EU is second only to that with the US while for the EU. China is its largest trading partner and second largest source of imported goods after Japan. In 2009, the EU exported 87.1 billion euros worth of goods to China and imported almost 215 billion euros worth of mainly industrial and manufactured products from China. Some 50% of China's GDP and almost 90% of EU external trade depends on shipping⁶³. Anything that impacts on the maritime transport of raw materials,

industrial and manufactured goods into and out of the ports of China and the EU could cause significant economic harm: climate change has the potential to have such an impact. This illustrates the interdependence of areas that might otherwise be seen as separate.

The UK Government's website, looking at the potential impact of climate change on sea levels, indicates that average sea levels may rise between 18 and 59 centimetres (or more) by the end of the 21st century, resulting in the inundation of some low lying island states and a greater risk of flooding in low lying areas which would put millions of people at risk⁶⁴. Other forecasters have suggested potential sea levels rises of many metres but any rise may result in loss of land, changes in maritime storms and an increased risk of severe weather incidents, together with implications for water resources, loss of homes, increased risk of water-borne illness and, in the context of maritime trade, damage to or loss of major seaports.

McKinney, in a study of the impact on sea level rise on the Netherlands, one of the most densely populated countries in the world, illustrates the devastating effect such a rise might have in just one EU member state⁶⁵. The Dutch port of Rotterdam is the largest port in Europe with links to several large rivers including the Rhine and Maas, and a major hub for transport of goods into and out of Europe. Half of the Netherlands is less than one metre above sea level. Large areas of the country only exist as dry land because of the Zuyderzeeworks—a series of dykes –built to protect existing land and reclaim land, much of which is used for agriculture. In the event of a severe storm along the North Sea coastline, major flooding or damage to the dykes could result in severe damage to infrastructure, coastal erosion and loss of land, significant loss of life, and the need to relocate large numbers of people. It should also be noted that a one metre rise would also impact much of coastal Belgium, Denmark, Germany and the south-eastern seaboard of England, all where major ports are situated.

A similar one metre sea level rise in the Yellow Sea would threaten Shanghai, located on the mouth of the Yangtze river, and Tianjin, on the coast of the Bohai gulf. The National Bureau of Statistics of China puts the 2009 population of Shanghai at 19.21 million people and Tianjin at 12.28 million people⁶⁶. The economy in terms of total value of imports to and exports from those cities were US\$277 billion and US\$64 billion respectively. Shanghai alone accounts for almost 12.5% of the total value of imports and exports nationally. A comparison can be made between the potential impact of a one meter rise in sea level on Shanghai and the impact of the Three Gorges Dam project, started 1992 and completed in October 2008. That project cost approximately 15 billion euro (US\$ 22.5 billion), displaced approximately 1.2 million people and flooded 13 cities, 140 towns and over 1300 villages, together with the loss of large areas of fertile farm land. Resulting environmental problems from the dam include pollution entering the watercourses, deforestation and landslides in what is a geologically unstable region. Even if only small areas of Shanghai were to be impacted by flooding, ports and warehouses on the Yangtze, along with large populated areas would be affected. Sea level rise would therefore have a major economic impact on China, as well as an impact on human health, damage to coastal ecosystems and fisheries, contamination of groundwater and drinking water, and loss of habitable land.

The EU and China therefore both face potential significant damage to trade, economy and population from sea level rise. Cooperation in the areas of maritime transport and the marine environment is therefore vital to both. A number of cooperative activities are already in place. For example, the EU China Maritime Transport Agreement 2002 and its amendments of 2009, aims to strengthen and consolidate relations in the field of international maritime transport; strengthen cooperation on maritime security; promote multimodal transport (sea plus other transport modes) and increase efficiencies in the transport chain; allow free access to ports for cargoes and trade and equality for all operators; and develop a flexible, market oriented approach and economic benefits for both⁶⁷. This supplements governmental bilateral agreements and those between Chinese and EU companies on access to designated port areas to maintain a stable maritime trade.

EU-China cooperation in space also plays a role in the marine environment. The 2011 EU China Youth website, looking at international cooperation in space, highlights a number of areas of cooperation⁶⁸. The EU Global Monitoring for Environment and Security Initiative (GMES) uses a combination of satellites and ground based technology to monitor climate change and atmospheric or marine pollution. This system was, however, put to a very different use to support China's National Disaster Reduction Centre to provide lifesaving assistance to victims of a 7.1 magnitude earthquake in April 2010 through the use of high resolution photographs which helped lead rescue teams to survivors. That same system has the potential to be used in the event of tsunamis and severe weather events, both to locate survivors and also to identify damage to infrastructure and different locations. The EU is also cooperating with China on other major projects including DRAGONESS, a system to

exchange knowledge and expertise in marine monitoring for environment and security. The area of maritime transport is vital to both China and the EU. It is anticipated that cooperation will continue in future as maritime trade plays a major role for trade and the economy in both regions. While it is harder to predict how the EU and China will manage the environment and climate change to mutual satisfaction, both areas impact economic development and prosperity. For the EU, creating equilibrium is essential across the board. To do that, it will have to exploit multilateral opportunities both internally and in international fora.

6. Discussion

From this brief overview, it is clear that the EU and China are becoming ever more engaged as trade and economic stability are vital to both in terms of the importance each play as trading partners and the economic stability which can arise from this. However, they are also competitors in the world market for oil, food and raw materials. There are continuing areas of tension where progress beyond symbolic levels is best achieved via quiet, multilateral diplomacy. History provides a potent illustration of this in the symbolic 'arms embargo' imposed to indicate EU members' concern at the repression of human rights at the pro-democracy demonstrations in Tiananmen Square in June 1989. The British House of Lords noted that this was not an arms embargo in the traditional sense (as it excluded a list of proscribed technologies or weapons which would normally form part of a serious embargo) but was basically an interruption of military cooperation and arms trade with China subject to non-binding differential approaches of each EU member state⁶⁹. It was limited to goods that might be used by the Chinese for internal repression, and did not stop arms sales by EU member states. The Lords report noted that:

'The embargo is an acutely sensitive and symbolic issue for the Chinese and a constant irritant in EU-China relations... the EU refuses to lift the embargo and [the Chinese] regularly raise the issue... While lifting the embargo would be politically symbolic, the EU has more effective legislation in a Common Position on arms exports, which is legally binding on all Member States. It applies to exports to third countries and does not therefore single out China.'

The EU also has a Dual-Use Regulation which controls the export of sensitive technologies to China and other countries which is potentially significant if difficult to implement⁷⁰. The House of Lords concluded that the EU should be prepared to lift the arms embargo only when the international conditions above have been fulfilled and if the Chinese government makes progress on human rights and regional security. Specific conditions should include ratification of the International Covenant on Civil and Political Rights, greater transparency on military modernisation and the removal of the military threat to Taiwan.

There is scope for increased cooperation to ensure that the EU and China maximise their opportunities to develop, through the tools of multilateral diplomacy at all levels, their potential for influence on the world stage and regionally and for trying to develop standards across the range of activities and policy areas. They share an interest in working on trade and customs issues to combat organised international crime, fraud, piracy and counterfeiting. They are well-positioned to play important roles in regional settings to help shape future policies and maximise opportunities for promoting cooperation with regional organisations on matters of common interest⁷¹. Regional engagement allows for misunderstandings to be explored and compared to overcome preconceptions, including perceptions of Chinese reticence to sign up to international accords, WTO and UN agreements valued by the EU⁷². The EU continues to fund many region-to-region capacity building and region-to-region cooperative initiatives of which China is a beneficiary⁷³. The emphasis in these programmes mirrors some of the issues that for China and the EU are priorities: climate change and energy. Others include health, migration, education and culture and cooperation and policy reform in the area of security. Cooperation with China has shifted from emphasis on infrastructural capacity building and rural development programmes to support for socio-economic reform, sustainable development, good governance and the rule of law. EU funding has gone to non-profit making bodies in education, trade and investment, human rights and the environment⁷⁴. Similarly, cultural region-to-region vertical and horizontal multilateral diplomacy helps to foster and exchange experience. This was done in 2009 through the Forum on China-Europe Cultural Industries – a high-level international summit forum – jointly hosted by China's Ministry of Culture, Ministry of Commerce, State Administration of Radio, Film and Television, General Administration of Press and Publication, the China Council for the Promotion of International Trade (CCPIT), Guangdong Provincial People's Government, Shenzhen Municipal People's Government and General Division of Education and Culture of European Commission. It was organized by the Organizing Committee of China (Shenzhen) International Cultural Industries Fair and Shenzhen International Cultural Industry Fair Co., Ltd⁷⁵.

This shows that using multilateral diplomacy and forums in which multilateral negotiation and dialogue can be expanded and developed is a productive way of promoting cooperation and understanding⁷⁶. Moreover, the EU provides a useful example of how the strategy of multilateralism can be developed to realise internal domestic goals. The example of EU integration, and the gradual processes of mutual accommodation and harmonisation that the supranational approach to policymaking and regulation initiated, could be helpful in enabling China to develop an approach to overcoming its highly fragmented internal market. This would benefit China's economic development and would also enable the EU and China together to surmount increasing difficulties for EU business and commercial interests trying to negotiate that fragmentation and avoid consequential misunderstanding. Following the European model is something that yields mutual advantages both in this area and in that regarding consumer goods and product safety. Similarly, exploiting the opportunities to promote greater mutual understanding through formal programmes on cultural and educational exchanges (such as Erasmus Mundus) and initiating dialogue on social and economic affairs, employment, labour regimes and practices through Memoranda of Understanding on social protection (again influenced by the European experience) provides a rich source of future collaboration.

To conclude, this chapter provides a brief snapshot of a range of areas where there is cooperation between the EU and China. It shows that those areas are not necessarily ones that are expected, and that thanks to multilateralism cooperation has, and will, continue to develop in the future.

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Chapter 3

China within the emerging Asian multilateralism and regionalism as perceived through a comparison with the European Neighbourhood Policy

Maria–Eugenia Bardaro and Frederik Ponjaert

1. Introduction

Although the People’s Republic of China’s (PRC) new found international significance has been widely commented, such analyses have tended to focus on global systemic implications¹; specific bilateral implications²; or internal resources³. Only recently has a series of mid–level analyses started to assess the PRC’s distinct impact on the regional scene. It seeks to identify how Beijing’s choices will come to shape the distinctive structural features and key policy dynamics of the emerging Asian multilateralism and regionalism. Within this context, the question as to whether the PRC has developed a distinct and identifiable ‘*Neighbourhood Policy*’ – akin to the efforts deployed by the EU in its own backyard – would certainly contribute towards better understanding the regional implications and calculations associated with the PRC’s rise. In seeking to unpack the PRC’s macro–regional approach, this analysis will strive to identify whether China has over the past decade(s) come to develop a coherent set of policies aimed at identifying and organizing its neighbourhood(s) in a multilateral fashion. Furthermore, if such a ‘*Chinese neighbourhood policy*’ can be isolated, it is most likely to be characterized by a distinct set of goals and means rooted in its specific relationship to the State and its borders. This chapter therefore sets out to verify the hypothesis that the PRC has generated a specific “*Asian Neighbourhood Policy*” with milestones and methods that are akin to the “*European Neighbourhood Policy*”, but the underlying models of which are radically different.

2. The *European Neighbourhood Policy*: An Original Comparative Template

Within comparative regionalism, an important share of the literature contrasts East Asian and European experiences of regional cooperation. This body of work has established that both regions have over the past decades experienced in varying fashions a common trend towards neo–regional cooperation. This rise of ‘*regionness*’⁴ is a shared global dynamic with very distinct regional expressions⁵. Overarching systemic comparisons can establish said common orientation, but fully understanding the underlying distinction between Europe and East Asia requires more focussed, mid–level policy–based comparisons. A promising policy–lens which remarkably has rarely been used up to now is the notion of *neighbourhood* which carries with it insights into region–building and is premised on a transferable notion of *proximity*.

2.1. A Return to Multi-polarity: Ordering Interdependencies through Regions?

If the antiquatedness of the Cold War bipolar system is well established in the literature⁶, the exact nature of the subsequently emerging international logic(s) has become the core controversy within international Relations (IR) studies of the past 3 decades. Commonly accepted evolutions within the international system such as (1) *growing interdependencies*⁷, (2) *new emerging powers*⁸, (3) *diminishing distances*⁹, (4) *the increasing free flow of information and technology* or (5) *the accelerating impacts of deepening economic globalisation* – have invariably been seen as both possible sources of enhanced cooperation, as well as potential new risk factors.

With the dissolution of the stifling yet equally ordering straightjacket of the Cold War, a wider range of dynamic variables and uncertainties came to the fore. Beyond the paradigmatically distinct critical approaches, systemically-oriented IR debates have come to be driven by a rehabilitated dialectic between those systemic approaches stressing possible sources of ordering and cooperation; and those highlighting disruptive and conflicting forces. This opposition between what one can identify as a largely ‘*neo-Kantian*’ tradition, and a roughly ‘*neo-Hobbesian*’ one has over the past decades come to frame IR debates (see Table. 1)

Table. 1 Key-Postulates underwriting the structuring opposition between neo-Kantian & neo-Hobbesian readings

	Neo-Kantian	Neo-Hobbesian
Systemic driver of IR	Democratization & economic growth	Stressful security affairs and relative power
Primary instruments	Institutional arbitration & economic instruments	Military power & economic levers
Interdependencies imply	i. Decreased efficiency of military instruments ii. Confusion of policy priorities hierarchy iii. Growing Impact of exogenous factors on internal order	
Evaluation of implications of interdependencies	Opportunities for institutionalized Cooperation	Vulnerabilities as number of potential sources of conflict increase
Stabilising factor	Multilateral cooperation	Articulated power hierarchies

Whereas the determined European experience of five decades of regional integration is both conceptually and politically intimately linked to *neo-Kantian* approaches, the uneven and heterogeneous Asian multilateralism calls upon a multitude of conceptual and political discourses, the concerns of which tend to remain *neo-Hobbesian* at heart. Obviously pluralism and dissonant voices enrich the debate on both sides; nevertheless, both Europe and East Asia appear as the two key areas in the ongoing debate on the future of “regions in the global order”. Each of these two particular regional experiences have come to reflect one side of the fundamental debate in IR, whilst also proving to be the *loci* of some of the most innovative and enterprising regional efforts¹⁰. As a result, a comparative analysis of the European and East Asian experiences is of particular value as it confronts two determining cases, each reflecting different paths towards a shared result: increased regional cooperation.

In light of the fundamental opposition sketched above, the literature has increasingly sought to bridge the divide by focussing on mid-range theories aimed at illuminating specific governance efforts within a complex international system see-sawing between stability and change.

As the fluid, and even potentially chaotic, nature of the currently emerging international reality has become ever clearer, a significant segment of the aforementioned IR debate has focused on possible stabilizing factors which might contribute towards ordering the newly unleashed interdependent world order. If the first decade of the Post Cold War Period seemed to offer the vision of a short lived “*unipolar moment*”¹¹ centred on American hegemony¹², the subsequent decades have confirmed the premise of an increasingly complex international system. The result is an progressively more byzantine and less predictable world order marked by a multitude of interwoven seats of power with distinct points of reference. Assessing the People’s Republic of China’s (PRC) rise and its implications must therefore be done within the context of a *multidimensional international*

*scene*¹³ characterized by a number of *centres of relative gravity*¹⁴, and settled through a *plurality of cooperative institutions set up at varying levels*¹⁵. Accordingly, this paper limits itself to a single dimension: the implications of China's rise on the Asian Region as assessed through the institutional forms of neighbourly cooperation. As the regional strategies deployed by Beijing are unpacked through comparison, this paper hopes to offer a better understanding of their implications for the emerging Asian multilateralism and regionalism.

As older systemic approaches have been uprooted by changing realities, seemingly established dichotomies such as “West–Rest”¹⁶ or “North–South”¹⁷ have been challenged by evolving political realities. In contrast, the continued impact of geography, and in particular that of ‘*proximity*’, has emerged as a uniquely enduring independent variable which in various forms and intensities continues to play a central role in contemporary IR¹⁸. This has given a renewed meaning to historic tendencies to organize world affairs by regional poles. As homogenizing forces associated with globalisation have done away with past distinctions, both analytical as well as strategic thinkers have sought to re-affirm existing differences through regionally organized poles. ‘*Proximity*’ as an instrumental factor called upon by policy-makers – ranging from the 19th century *Monroe Doctrine* to the current *European Neighbourhood Policy* – enjoys a long tradition. Equally, as an analytical tool, ‘*proximity*’ has been both a consistent independent variable within all weighted models of economic integration – ranging from Balassa to current gravitational models of international trade, as well as a defining factor in the growing literature on (neo-) Regionalism.

A central organizing principle within the international system is thus the emergence of regional poles, each with its distinct centre of gravity and set of practices¹⁹. While Europe is the most developed form of regional cooperation and integration, most new and quite distinct sprouts of regionalization are found elsewhere, notably in Asia. Although this shared evolution towards prioritizing regional approaches founded on proximity has fostered a global neo-regional dynamic, its heterogeneous institutional consequences reflect its inherent diversities rooted in a wide range of region-specific factors. This analysis will compare the milestones, models and methods distinguishing China in its geographical vicinity to those mobilised by the EU in its neighbourhood.

2.2. Organizing Complexity: “Eclectic Institutionalism”, a workable framework wherein to examine the implications of proximity?

Having identified political ‘*proximity*’ as the definitive independent variable at the core of this analysis, both its methodological and conceptual choices need clarification. First and foremost, as understood in the long tradition of political geography, a given power’s ‘*neighbourhood*’ is conceived as “*a horizontal relation within multilevel governance characterized by proximity*”²⁰. Consequently, the milestones, models, and methods underwriting a given neighbourhood must be explained with reference to a multi-causal approach which recognizes the inherently multi-dimensional and multi-tiered nature of any given ‘*neighbourhood policy initiative*’²¹. Furthermore, as a product of political geography, a ‘*neighbourhood*’ is a political reality rooted in the geographical fact of *proximity*. However, geographic proximity alone is not an absolute and sufficient condition for the establishment of a *neighbourhood*²². It is above all a political construct and it is its institutionalisation which defines and demarcates it.

Bearing in mind these two intrinsic features of neighbourhoods – their complex nature and their necessary institutionalisation – the most operable conceptual framework appears to be an “eclectic” approach to the various schools of “institutionalism” as defined by V. Schmidt²³. At its core is a broader, more sociologically rooted and dynamic definition of institutions. These are understood as “*structures and constructs of meaning internal to agents whose ‘background ideational abilities’ enable them to create (and maintain) institutions while their ‘foreground discursive abilities’ enable them to communicate critically about them, to change (or maintain) them*”²⁴.

However, seeing the relatively novel nature of the study object itself – i.e. the notion of a *Chinese Neighbourhood Policy* (CNP) – its structural features and implications must be analysed before its internal dynamics can be ascertained. As a result, this specific inquiry does not seek to ‘*endogenize*’ the evolution of a prospective CNP, but rather define the contours and assess the structural characteristics of such a Chinese policy in relation to both the wider international system as well as other experiences of neighbourhoods.

As stated repeatedly, *neighbourhood policies* are to be understood as multi-tier and multi-dimensional institutionalized political processes aimed at a region defined by its *proximity*. The *European Neighbourhood*

Policy (ENP) appears as the most developed, discernible, and self-conscious example of a distinctive and integrated international governance effort towards a wider region. The ENP can therefore function as a heuristically useful point of comparison.

Such a comparison must be articulated around the key features of any cogent *neighbourhood policy*: the (1) *historically informed milestones* which define its long-term path dependencies; the (2) *models* which define its long-term norms and values and the (3) *methods associated* with the fixed preferences shaped by its long-term incentive structure. Identifying and describing each of these three dimensions within the ENP will produce a workable grid upon which to base our heuristic comparative analysis of the various components of China's policy initiatives towards its wider region.

2.3. Neighbourhood Policies: A Workable Comparative Framework?

2.3.1. Which (Reactive) Origins? The ENP: A Response to a Political Necessity

The end of the Cold War was a critical juncture of particular significance for the EC/EU. It led not only to a whole set of new countries seeking to join the EC/EU, but also to a strong demand for a more intensive European engagement in its wider region. The inherent constraints of the Cold War had implied that East and West on the European continent were separated by impermeable borders²⁵. This bipolar overlay served the Western Europeans well, for they could make the concept of "Europe" their own without having to consider either its boundaries or its Eastern proximity. However, since the end of the Cold War, the EU has continuously struggled with an existential dilemma born from its uncertain final borders²⁶.

The first reference to an EU neighbourhood policy can be found in a 2002 speech delivered by Romano Prodi, the former president of the EC. The Neighbourhood Policy (ENP) was then further outlined by the EC in March 2003 in "Wider Europe-Neighbourhood" and adopted by the Thessalonica European Council in June 2003. The ENP is first and foremost a response to the changing composition, shifting borders, and altered geopolitical outlook of the EU born from its eastern enlargement. The ENP is a framework for co-operation between the EU and its North African, Middle Eastern, Eastern European and Caucasian 'near abroad'. Russia has its own special relationship and is not part of the ENP. The common and central goal in relation to this whole group of countries is to promote a set of political, economic and security-related reforms.

Following the 2004 enlargement of the EU, previously distant countries would border the EU. The resulting sources of instability in its new near abroad were above all identified as relating to soft security concerns²⁷. Henceforth, the need for policy engagement with this newly defined space would be imperative. Although essential, the EU's engagement with its new near abroad would pose particular policy challenges as it would no longer be able to rely on its tried-and-tested regional governance mechanism: conditional EU accession²⁸. The ENP is clearly disconnected from the issue of potential EU membership. It offers a privileged relationship based on mutual commitment to common values such as democracy and human rights. Although, prompted by the need to find an alternative to EU membership as an international governance tool in its near-abroad, the setting up of the ENP was deeply influenced by the politics of eastern enlargement. Judith Kelley even quips that the ENP was fundamentally "*New Wine in Old Wine-skins*"²⁹. The development of said policy has been described as highly path-dependent and "*clearly modelled [...] on the enlargement process*"³⁰. Kelley also points out that the ENP methodology and terminology was inspired by the accession process. As such, the ENP was not developed with the neighbours in mind, it was "*the result of a process in which the EU was primarily concerned with itself*"³¹. The ENP represents a reassessment of the EU's external relations in response to fundamental changes within the EU itself.

To sum up, a quick historical institutionalist assessment of the ENP has allowed us to identify its path-dependent policy evolutions. Firstly, the ENP emerged in reaction to two critical junctures: the '89 end of the bipolar world, and the '04 enlargement. Subsequently, the ENP advanced mainly in reaction to key exogenous changes. Secondly, the historically determined governance models associated with the ENP are flawlessly in line with governance mechanisms associated with enlargement. Finally, its strategic orientations and preferences are dictated by long-standing internal dynamics which characterize the EU's own existential debate, and not considerations related to target countries.

2.3.2. Which (Blurred) Boundaries? The ENP: A Re-Definition Exercise

Since the creation of the EC/EU, the end-goal of its integration process has always been a matter of much contention. Attempts have been made to model the EU's evolution along the lines of existing state-centric models; the 'federalist' discourse rooted in 'Westphalian' state-centred understandings on the one hand; and 'imperial' readings centred on the domineering role of a core-Europe along similar lines as those linking core and periphery in world-system theories on the other. Others have sought to capture the *sui generis* dimension of the EU through novel concepts such as the 'neo-medieval' frame offering a fragmented and regionalised vision of a political order³². These various polity frames are defined by the level of power concentration, their inherent hierarchies and the scope of their sovereignty.

In the *Westphalian* perspective the EU is conceived in statist terms. The EU is seen as acquiring the most typical characteristics of a Westphalian state: diplomacy, army, hard external borders, etc. For example, the Schengen border regime can be understood as a statist-type border aimed at preserving the Union's territorial sovereignty vis-à-vis its neighbours. *Empire* is a concentric order emphasising core-periphery relationships based on political and economic power. Central here are ideas of the EU as "force for good"³³. The Empire frame entails a fuzzier understanding of the political space and its borders. Finally in the *neo-medieval* model the EU is defined through overlapping authorities, divided sovereignty, and diversified institutional arrangements wherein authority is shared. The Westphalian state evokes a set of cultural and political norms including relatively hard and exclusionary border lines, whilst both the neo-medieval and imperial frameworks involve open and fluid norms associated with soft border zones.

According to Zielonka "[t]he established scope and nature of EU borders will tell us whether the enlarged Union is likely to become a Westphalian superstate or something entirely novel"³⁴. Neighbourhood thus becomes a key factor as well as a symptomatic indicator of the underlying models distinguishing the European experience of regional multilateral cooperation.

Borders are not simple lines on maps; they can represent an area of division and demarcation, or alternatively one of contact, exchange and integration. As Zielonka points out borders are complex institutions³⁵. In his opinion, the EU is unlikely to be defined by a set of rigid and impermeable borders³⁶. Indeed, the Union seems to be evolving towards a "maze Europe"³⁷ with less territorial, less physical and less visible borders³⁸. In this sense, EU's borders will probably resemble the borders of a neo-medieval Europe rather than a Westphalian Europe³⁹.

The ENP can be analysed as an attempt to transform the EU's borders from areas of demarcation and division into zones of exchange and interaction, thus overcoming the *inclusion-exclusion* logic. The ENP's central agenda is geared towards cultivating development and exchange within border-regions so as "to prevent the emergence of new dividing lines"⁴⁰. The ENP aims at tying its old and new neighbours closely to the EU while simultaneously interconnecting its various neighbours. In conclusion, the ENP offers some insight into the models shaping the EU's polity. In this sense, the EU's interpretation of the outer limits of its polity resembles the open-ended *imperial* and *neo-medieval* frameworks, rather than the hermetic borders of a Westphalian state. Although the ENP is clearly animated by a fluid and open understanding of the relationship between the inside and the outside of a polity, this does not mean that the EU's polity will necessarily evolve towards a neo-medieval or imperial model. However, the ENP reflects the EU's awareness that entrenching borders will not only diminish the EU's attractiveness but also feed the perception of the EU as a fortress.

2.3.3 Which (Managerial) Methods? The ENP: A Policy Set to Govern Risks and Opportunities.

In order to conceptualise different facets of the EU's approach to its evolving *neighbourhood* we will here refer to the framework developed by Walters (2004). He identifies four main types of neighbourly relations: (1) the *networked (non-)border*, (2) *the march*, (3) *the colonial frontier* and (4) *the limes*. According to Walters, each of these geo-strategic ideal-types identifies a given approach to border regions. To identify particular geo-strategies is not to assume that these aspirations are necessarily fully accomplished. *Geo-strategy* is understood as "a particular way of organising the space of the border. It presupposes many things, including particular definitions of the inside and outside, the type of threat or problem which the border is to address, and the specific accounts of the time and the space of the border"⁴¹.

The first *geo-strategic ideal-type* is the one that resonates with the themes of de-territorialisation and a borderless world. *Networked (non-) borders* offer renewed incentive structures wherein traditional border controls are replaced with new forms of regulation. As Walters points out, “*this term is meant to convey the sense in which networks of control come to substitute for the functions that were previously physically concentrated at the border*”⁴². This geo-strategy does not identify a clear demarcation between inside–outside. It incentivises sharing responsibility with outsiders and it emphasize a non-traditional and non-spatial view of borders.

The *march* is an archaic name which in many ways pertains to a pre-modern understanding. It was common, instead, to find the *march* as a neutral demarcation strip or belt. According to Walter, the *march* is an inter-zone between entities; a buffer zone which aims to protect and insulate the interior. A second pre-modern understanding of borders, steeped in the roman imperial experience, is that of Limes. According to Walters , “*if the space of the march is a area between powers, an interzone, and that of the modern frontier a finite line demarcating and separating territories, then the limes is more like an edge, fringe or limit*” aimed at maintaining the distinction between stability within and the disorder without⁴³.

The final two geo-strategic ideal-types are two opposite evolutions of borders within the modern system. A (*colonial*) *frontier* is a transformative and dynamic space. Central to this *geo-strategic* model is the potential for transformation of the outside with an eye on making it more similar to the inside even to the point of assimilation. Asymmetrical relationships are set up in which the expanding power assumes a right to define that which is appropriate and just. In contrast, the classical Westphalian border does not seek to organise the projection of an internal agenda on to the neighbouring outside, but seeks to insulate the inside from any external influences.

The distinctions made by Browning and Joenniemi⁴⁴ as well as the clarifications proposed by Anderson⁴⁵ allow for a better understanding of the incentive structures shaping the ENP and other approaches to *neighbourhood* (see table 2.).

Table. 2: Overview of possible frameworks and incentives structuring a neighbourhood policy

Geo-political Model	Geo-strategy	Vision of the Outside	Underlying Dynamic	Relative Relationship
Imperial	<i>(colonial) Frontier</i>	<i>Transformative Opportunities</i>	<i>Outward</i>	<i>Unequal</i>
	<i>Limes / March</i>	<i>Threats of Instability</i>	<i>Inward</i>	
Westphalian	<i>Modern Borders</i>	<i>Risk Management and containment</i>	<i>Inward</i>	<i>Equal</i>
Neo-Medieval	<i>Networked (non-) Border</i>	<i>Transformative Opportunities</i>	<i>Outward</i>	<i>Equal</i>

The ENP effort to create a ring of friends is aimed at securing the EU’s external periphery. This can be seen as an attempt to create a buffer zone between the EU’s inside and outside⁴⁶. Through a ring of friends, the EU conveys a centre-periphery approach, which suggests that the main incentive is not the establishment of a network in which all actors are equal but rather a concentric system in which Europe is at the core. Such defensive structures stand in sharp contrast with the oft re-affirmed principled references to “*shared interests*” and “*joint ownership*” presented in the official ENP documents. The outside is therefore conceived in threatening terms. Such calculations seem to favour a *Limesor March* rationale.

In conclusion, the ENP also reflects the EU’s constant perception of its *neighbourhood* as a source of opportunities. Seizing said opportunities has been the second incentive at the core of the ENP, whether they are to be established jointly through networks or unilaterally through unequal power projection. Yet as the ENP was from the onset conceived as an alternative to enlargement, its *frontier* logic therefore remains incipient at best. Structurally the ENP favours joint ownership and networked cross-border initiatives when seeking to profit from its *neighbourhood*. Accordingly, long-term institutionalised rational choices have moulded the ENP into a geo-strategic approach to the EU’s *neighbourhood* which tends towards a *March* type when threats are seen

as prevalent, and towards a *network* logic when opportunities are seen as more important. Variations are the result of case-by-case calculations unilaterally dictated by the EU as a function of the geographical position of the borders and relative concerns associated with it.

3. China's Southern Periphery: Assessing its Approach to ASEAN

3.1. The Relationship's Historical Roots: Clay or Rock Foundations?

For centuries China's regional environment at regular intervals had a rigid hierarchical and hegemonic structure with China at its centre. This Sino-centric world order was based on a clear distinction between civilization (China) and barbarians. In order to contain and isolate barbarian threats, Chinese emperors employed both fortification and a singular form of diplomacy – the “*tributary system*”⁴⁷. Beyond the Middle-Kingdom – the “first circle” of the Chinese World Order – the barbarian-vassals who had accepted and partially assimilated the values of the Chinese (Han) civilization would send tributes to the Chinese emperor as a sign of their acceptance of suzerainty⁴⁸. These “second circle” barbarian-vassals, situated at the periphery of the Empire, provided a *march* (buffer-zone) ideally suited towards checking potential threats arising from beyond the Middle-kingdom's direct reach. However, when vassal-barbarian states or groups challenged the centrality and superiority of the Chinese civilization, hegemony had to be restored through direct or indirect Chinese intervention⁴⁹. Situated in “the third circle”, the outmost barbarians or “*yi*” were located beyond the “second circle” of vassal-barbarians. This group was perceived as relatively irrelevant due to both their ‘inferior’ nature and their remoteness. Accordingly, China's environment was written into one of two policy paths: in its close proximity a population awaiting relative assimilation into the Chinese world; and beyond that, a relatively inconsequential thron to be benignly neglected⁵⁰. Such an hierarchically and anti-egalitarian world order was therefore characterized by the absence of sovereign State to sovereign State relations.

Most South-East Asia States were part of the Sino-centric “*greater inter-state system of the China seas*”⁵¹ which allowed them to send tributes to the imperial court and trade in permitted areas in China. More specifically, the historical determinants of China's relations with SEA were geographic proximity, monopolistic trade exchanges, ethnic communities and political links. Due to their continued symbolical importance, these historic imperial practices are still shaping the PRC's definition of its proximity or “*regionness*”; but they do not weigh on its modern experience thereof. First colonialism, then modernity and finally the Cold War wholly removed all the foundations of the ancient imperial tributary system.

In particular, China's Cold War support for communist insurgencies in the region was a key factor in creating negative feelings and hostility towards Beijing among the non-communist SEA states. As a result, the end of the Cold War represented a propitious juncture for the emergence of a renewed proactive Chinese engagement towards SEA. For both ASEAN and China, the early '90s were characterized by mutual suspicion regarding their respective interests and intentions; but this period also marked an ever more recognized need to reconsider their relationship. China's strategic imperatives were twofold: to secure its southern periphery and to prevent the creation of a containment coalition. Hence, Goldstein's assessment of a need for a neo-Bismarkian great strategy focused on both preventing forces emerging against China, and securing sufficient time to concentrate on the country's internal development⁵². Moreover, China's regional engagement is based upon maintaining “harmony” in domestic affairs. Domestic stability is one of the major prerequisites for, and conditions of, China's successful economic development. Contemporary China's general attitude towards the world is characterized by the philosophical concept “*he erbutong*” – seeking harmony but in keeping with its own distinctiveness⁵³. After the open door policy gained ascendancy in 1978 and China re-entered the world community, the “*general attitude towards the world order changed from the notion of nishini, woshiwo (you are you, I am I) during Mao Zedong's era, to Deng Xiaoping's new he erbutong approach*”⁵⁴. In Beijing's eyes, this implies a stable international order composed of Westphalian states. Accordingly, the neighbourhood policies developed since have conformed to these principles. On the one hand, China has moved from relative isolation to State-to-State enhanced dialogue and on the other, domestic affairs remain excluded from said dialogues.

Ambiguities regarding China's position within the world system it had just fully joined remained: would China be a reformist or a revisionist power? As this threat-perception of China's rise gained increasing traction in SEA⁵⁵, it became a major consideration of China's early Neighbourhood Policy. Chinese leaders such as HuJintao have championed political frameworks emphasizing that China's rise is everything but a threat. The notions of peace

and development (*hepingfazhan*), peaceful rise (*hepingjueqi*) or harmonious world (*hexieshijie*) primarily indicate the desired benign orientation of Chinese foreign policy. In spite of these official statements regarding China's future path, whether China's affirmed choices are either fundamental or merely rhetorical remains to be seen⁵⁶. Despite this uncertainty, the political situation in Asia has been rather stable in the last two decades. As David Shambaugh states, “[t]oday, China is increasingly seen as a good neighbour, constructive partner, and careful listener. Importantly, it is also increasingly multilateral in its diplomacy”⁵⁷.

To raise trust and reduce regional threat perceptions of China, Beijing began in the early '90s a policy of “neighbourliness, trustworthiness and partnership” with neighbouring countries⁵⁸. In 1993, then Chinese Premier Li Peng noted that “*active development of beneficial and friendly relations with neighbouring states, in striving for a peaceful and tranquil surrounding environment, is an important aspect of [China] country's foreign affairs work*”⁵⁹. This statement may be considered a foundational moment for China's Neighbourhood Policy.

The above developed institutional–historical analysis identifies the South East Asian dimension of a possible Chinese Neighbourhood Policy (CNP) jump started by two critical developments in the early 90's: a new favourable post–Cold War regional environment, and the compelling worries relating to China's increasing regional prominence. More specifically, Beijing's fostering of a “good neighbour policy” reflects its willingness to present itself, both regionally and internationally, as a cooperative and non–threatening country. If the European Neighbourhood Policy is a clear reaction to the '89 and '04 turning–points, the South East Asian dimension of a CNP would be defined as a gradual response to new exogenous opportunities and threat perceptions. While the initial set–up of China's approach to SEA can be explained as a result of changed external factors, its subsequent strategy and development are the result of both internal and external dynamics. This stands in contrast to the ENP where both its set–up and its subsequent policy developments are almost exclusively dictated by internal EU concerns and policy debates. Finally, while the ENP is deeply entrenched in policy paths inherited from the enlargement process, China's approach to the SEA is a key feature of China's ongoing effort to redefine its international position (see Table 3).

Table 3: Historical Dimensions Compared: the ENP and China's approach to SEA

	Critical–Juncture & Catalyst	Policy–Paths	Drivers of Cooperation
ENP	Critical–Juncture '89 – Systemic Revolution Catalyst '04 – Enlargement	Policy Mechanisms inherited from enlargement processes	Endogenous Policy Debates
China's approach to SEA	Critical–Juncture '89 – Systemic Revolution Catalyst Early '90 – Threatening perceptions of China	Experimental ASEAN–compatible “Regionalist” processes	Endogenous Political Ambitions & Exogenous Perceptions of Uncertainty

In conclusion, one might state that the ENP, as a securely established set of reactive policy practices, has been built upon ‘stone’ foundations. The EU and its neighbourhood have derived a significantly heightened sense of certainty and predictability from the ENP. However, all players have been locked into rigid and often unresponsive practices. On the contrary, the ‘clay’ foundations of China's SEA policies are the result of a gradual build–up of initiatives jointly driven by domestic and related concerns. This has resulted in a flexible, adaptable and non–threatening policy–set. However, such policy initiatives have failed to provide the region with significantly increased predictability, thus leaving unanswered most fundamental reservations regarding China's future role in Asia.

3.2. Mutual Perceptions: From Another's Cold–Shoulder to a Community's Warm Embrace?

Over the past decades an increasingly well–established China–ASEAN relationship has come to define China's approach to its southern periphery. Such a recognizably institutionalized relationship implies a set of shared models and accepted methods.

As the suspicions that once defined the ASEAN–China relationship started to ebb, mutual cooperation became possible. This emerging neighbourly relationship quickly took off and expanded following both systemic changes and deliberate Chinese trust–building efforts born from China’s re–assessment of its own regional interests. In the early ‘90s, as it took an increasingly positive approach towards regional institutions, China first became ASEAN’s ‘consultative partner’ in ‘91 and was subsequently promoted to ‘full dialogue partner’ in 1996. Two years earlier, China had already joined the regional security dialogue through the ASEAN Regional Forum. Sino–ASEAN dialogue was subsequently institutionalized with the creation of five dialogue mechanisms in the areas of politics, research, innovation, economics and trade.

The ‘97 crisis was not a turning–point in China’s approach to South East Asia. For Southeast Asia, the 1997 financial crisis remains the key regional turning point of the post–Cold War period, and China’s reactions at the time contributed greatly to improving perceptions of Beijing’s positive regional role. Its US\$1 billion aid package to Thailand, assurances not to devalue the Yuan, the extension of trade credits and offers of Financial aid were all welcomed as signs of Beijing’s earnest desire to play a constructive leadership role in the region. Concomitantly, ASEAN hopes that China would continue to open its market to help enhance the slackening demand for ASEAN exports were fulfilled as Beijing jump–started the China–ASEAN FTA negotiations. By this point, ASEAN has already emerged as the 4th largest export market for China.

Further positive steps in the China–ASEAN relationship include China’s signing of the protocol to make Southeast Asia a nuclear–free zone (ZOPFAN) in 2001, its willingness to negotiate the Spratlys dispute through ASEAN, and its formal subscription to the ASEAN treaty of amity and cooperation in 2003. Engagement and dialogue have also taken place bilaterally between China and ASEAN through the ASEAN–China Senior Officials Consultations, ASEAN China Joint Cooperation Committee meetings, ASEAN+China framework and regular ASEAN–China summits. Step–by–step, through trialand error, but on the basis of clearly identified principles, ASEAN and China have sought to build up and institutionalize a shared neighbourly community.

A pioneering effort in regional community–building in Asia, ASEAN was established in ‘67 as a cooperative security initiative, based on reassurance through dialogue and not military deterrence. Rather than impose sanctions, develop “*conditionalities*” or specific functional problem–solving measures, ASEAN has consistently relied on the promotion of agreed norms and principles to regulate its members’ behaviour⁶⁰. This had led to the emergence of an ASEAN–way discourse on regional multilateral cooperation. This was developed in opposition to both the fatalistic neo–Hobbesian conclusions regarding the likelihood of transformational cooperative outcomes in institutions, and the hubristic neo–Kantian drive towards institutionalized integration⁶¹. The ASEAN way rests upon a constructivist understanding of the socialisation process, arguing that a regional community can be fostered through formally weak institutions (through familiarity, consensus, consultation, non–coercive argumentation, and avoidance of legalistic rigours with regards to distribution problems in favour of case–by–case arbitration) as the process itself can produce the desired cooperative outcomes with multilateral institutions⁶². This ‘third way’ suggests the endogenous interactive social effects of institutions can lead to high levels of cooperation with low levels of intrusiveness and formality.

The decade–long experience of ASEAN in the field of regional multilateral cooperation that is informal, non–confrontational, reciprocal, non–intrusive and thus respectful of its underlying Westphalian premises was increasingly recognized in Beijing, as its own interest in multilateralism grew. The ASEAN–way’s defining legal–normative regional model meshed perfectly with the Westphalian state model championed by Beijing. The principles of (1) prohibition on the use of force as a dispute settlement; (2) the recognition of a certain autonomy at the regional policy level which is not to be a mere secondary discussion venue; (3) and an absolute respect of the principle of non–intervention quickly emerged as shared foundations on which to build a solid socialization process of China’s multilateralist strategy within its South East Asian neighbourhood policy⁶³.

China’s engagement through its South East Asian neighbourhood with a growing number of multilateral forums (ASEAN, ARF, ASEAN+3, etc.) involving a growing number of fields has helped to sensitize China to the realities of multilateral cooperation. This encourages normative convergence regarding preferred forms and outcomes of regional cooperation. China’s continued involvement in these regional forums – for more than a decade – confirms the progressive institutionalisation of newly socialized behaviours. Whatever China’s initial calculations might have been, its South East Asian Neighbourhood policy has become the main *locus* where Beijing has crystallized those cooperative methods it deems most appropriate with regards to regional community–building.

The crux of China’s pursuit of “amicable, peaceful and prosperous neighbours” lies in its new approach to multilateralism (*duojihua*), both at the global and regional levels⁶⁴. Beijing has increasingly incorporated a multilateral perspective focussed on promoting State stabilisation and sovereignty consolidation; enhanced mutual trust through confidence–building measures and reduced uncertainties; and multi–faceted cooperation in any policy field of common interest. In this manner the Chinese leadership has increasingly strengthened its relations with its South East neighbours through regional multilateral economic and security institutions⁶⁵.

The socialization within the China–ASEAN nexus regarding methods of regional multilateral cooperation contributed towards shaping China’s emerging synthesis between its continued attachment to Westphalian sovereignty and the cooperative necessities born from Beijing’s rise and its associated emerging Grand Strategy. China’s relation with ASEAN States challenges ancient categorization such as centre–periphery or lord–vassal. These Chinese Neighbourhood policies in themselves illustrate the growing propensity for decisions on issues of common interests to be taken within multilateral arrangements. This represents a shift in China’s regional relations towards its neighbours and a significant contribution towards the emerging Asian multilateral and regional practices.

In its threat–centric perception the EU has come to mainly perceive its neighbourhood as a necessary buffer–zone preventing negative spill–over. This has proven particularly true with regards to its southern borders. In contrast China sees its southern borders as sufficiently resilient as such. It has therefore focused on developing cooperative methods which bridge the borders without weakening them. Consequently, borders between China and its ASEAN partners remain unchanged in nature, but their isolating effects are mitigated through cooperative processes which are deemed useful in reducing the inherent uncertainties associated with cross–border relations. China’s South East Asian Neighbourhood policy discourse essentially represents cross–border cooperation, common interest and mutual trust. Through such egalitarian bridging methods the Chinese neighbourhood policy seeks to strengthen the states’ modern Westphalian borders, whereas the ENP’s practices seek to consolidate its polity through a reinvention of buffering logics akin to *Marches*. Surprisingly, the ENP seems more imperially inclined towards its neighbourhood than China’s neighbourhood policy (see Table 4).

Table. 4 : The “Neighbourly” Models and Methods Associated with the ENP and China’s ASEAN policy

	Perception of the Outside	Geopolitical Models	Geostrategic Methods	Cooperative Dynamics	Relative Relations
ENP	Threat	Imperial	Limes/March	Consolidate	Unequal
	Opportunity	Neo–Medieval	Networked	Cooperate	Unequal
China’s approach to SEA	Risk containment	Westphalien	Modern Borders	Insulate	Equal
	Risk management			Bridge	

In summary, as South East Asia becomes involved in the region–building effort, China’s is increasingly becoming a constructive contributing factor. The EU, with the ENP, appears to have marginalised the regional dimension in its approach to its neighbours in favour of differentiated bilateralism. Operating on a bilateral basis, the EU through its ENP is *cold–shouldering* any attempt with its neighbourhood towards *regionness*. On the contrary, and more strikingly, China’s has warmly embraced South–East Asian regional community–building efforts. Chinese approach is more focussed on long–term structural considerations, whereas various short–term threat–considerations dominate the ENP. Finally, the fact that China’s engagement has persisted beyond its initial inception confirms the emergence of a consistent Chinese practice of multilateralism through regionalism.

4. China's Northern Peripheries: Confronting its Central and Northern East Asian Strategies

4.1. The Relationships' Historical Roots: Clay or Stone Foundations?

When addressing China's historically fraught relationship with its northern peripheries one must first and foremost factor in a *longue durée* perspective so as to grasp the deep-seated historically determined elements. Akin to the dynamics identified vis-à-vis South East Asia, Chinese perceptions and demarcations of its northern periphery are the product of well entrenched historically-influenced neighbourhood discourses and relations. The above described imperial order which affected China's neighbourhood for millennia was obviously also at play in its northern periphery. Nevertheless, some important distinctions can be made.

Historically a northern periphery can be identified as part of the more or less stable "second circle" ensconcing the Middle-Kingdom. Beijing's understanding of the contours of its "proximity" continue to be forged by the repeated historical practices related to "the nature and linkages of China's past tributary system"⁶⁶. "[F]irst, the Sinic Zone: consisting of the most nearby and culturally similar territories, Korea and Vietnam, the Ryky Islands, and, at brief times, Japan; [s]econdly, the Inner Asia Zone: tributary tribes and states of the nomadic or semi-nomadic peoples of Inner Asia, who were on the fringe of the Chinese culture area"⁶⁷. A two-fold northern neighbourhood has historically occupied the minds of Chinese leaders wherein distinct principles, practices and institutions tended to differentiate between Central Asia on the one hand, and North East Asia on the other.

In its dealings with Central Asia – where the Chinese culture-based theory of hegemony had to come to terms with the geographical fact of nomadic inner Asian fighting powers – the use of force became the rule rather than the exception⁶⁸. In contrast, Chinese relations with its North East Asian Neighbouring states (i.e. Japan, the successive Kingdoms of the Korean peninsula, and the Ryukyu Kingdom) were more readily recognized as tributary⁶⁹. China's relationship with its North East Asian neighbours was however more erratic than with its South East Asian tributary states, as it would experience periods of deep engagement separated by interludes of mutual withdrawal. Such phases of relative disconnect could even last for centuries, for example two-and-a-half centuries in the case of Japan's Tokugawa Shogunate. Both of China's historically defined groups of northern neighbours have long-established linkages with China, but their specific nature is typified by distinctive *cyclical* dynamics. A broader tradition of violence and invasion has regularly disrupted China's Central Asian neighbourhood; whereas a succession of entanglement and disengagement phases have proven to be the premises of a more volatile relationship towards North East Asia.

Current Chinese neighbourly relations were born in denial of empire, but their medium-term perspectives are oft influenced by a bi-millenary imperial legacy⁷⁰. Accordingly, imperial legacies can help explain China's instinctive delimitations of its northern neighbourhood. However, its contemporary nature and developments are to be understood within the current international context. Interestingly, the '89 systemic revolution had a very unequal impact on the realities facing China in its northern periphery. If the fall of the USSR can undoubtedly qualify as a systemic shift of critical proportions in Central Asia, its North East Asian impact was quite limited.

The end of the Cold War allowed for renewed opportunities for cooperation in Central Asia as old divisions and encrusted enmities were removed with the dissolution of the USSR⁷¹. Following the '89 critical juncture, both South East and Central Asia witnessed a marked increase in the depth and breadth of Chinese engagement. Subsequently however, both regions saw their paths with regard to cooperation with China diverge. If the end of the bi-polar world opened up the possibility for China to develop a new approach to its Central Asian neighbourhood, only in 2001 did said exercise gain political traction and institutionalized practices. The first decade of the relationship between China and its four most important partners in Central Asia – i.e. Kazakhstan, Uzbekistan, Tajikistan, and Kirghizstan – was highly informal, loosely oriented towards security concerns, and mainly explorative in nature. As such, the so-called *Shanghai Five Grouping* launched in '96 is to be seen as an initial trust-building and re-acquaintance exercise following the '89 upheavals. The '01 American invasion of Afghanistan was the main catalyst behind the subsequently institutionalised Chinese neighbourhood policy towards Central Asia⁷².

With the so-called *Shanghai Cooperation Organisation* (SCO), Beijing launched a strategic and coherent central Asian *neighbourhood* policy responding to the twin challenges of an ever more encroaching American presence, on the one hand; and a heightened international anti-terrorist agenda, on the other. The SCO's development has been relatively isolated from the two other sub-regions⁷³. It has been mainly driven by exogenous and systemic factors. Clearly construed as a classical intergovernmental multilateral organisation, the SCO is locked into accommodating forms of interactions. Said interactions are strategic, reciprocal, unanimous, and highly contextual. The SCO's policy path is not the product of a Chinese re-prioritizing or re-assessment of its central Asian proximity as such, but rather an offshoot born from the confrontation between China's emerging global geo-strategy and exogenous factors in its own backyard. As a result, China's interaction with its Central Asian neighbourhood has been essentially a derivative dynamic.

North East Asia in contrast remained remarkably unchanged by the end of the Cold War. The major North East Asian Cold War sources of conflict, their symbolic disputes, and sources of distrust all survived the system that produced them⁷⁴. These vestigial Cold War traces have prevented a deep Chinese engagement from gradually emerging. The North East Asian dimension of China's Asia strategy is thus deemed to have only evolved under duress, towards a 'stunted regionalism'⁷⁵. Without any clear critical juncture which fundamentally "re-shuffled" the cards between China and its North East Asian periphery, the main concern has been stabilising the status quo in spite of powerful exogenous and endogenous transformational forces. Chinese efforts are aimed at either reaffirming the viability of the status quo (series of bilateral and trilateral '*summitting*') or bringing it up to date by often belatedly inscribing it into broader regional dynamics which are defined and shaped elsewhere (i.e. the ASEN+3 process leading ultimately to the prospects of an EAC).

Joint reaffirmation of the status quo tends to be the standard response to endogenous destabilizing forces born from within the domestic polities involved. As such, it has become a nearly ritualized form of reconciliation and reassurance, most recently deployed following the 'eventful' premierships of the PM Koizumi in Japan⁷⁶. This highly symbolic 'return' to dialogue after a period of relative dismissal is a structural feature of China's North East Asian relationship. This cyclical process of dismissal and re-acquaintance has been a constant feature of China's North East Asian policy path, be it during the Cold War (e.g. the tensions surrounding the Nakasone Premiership), during the fluid years marking its demise (e.g. the hardening of relations following the Tian'anmen incidents), or since the emergence of new forms of Asian multilateralism (e.g. the repeated cycles of the 6-party talks since '03).

The second motor of China's North Asian efforts has been a shared will to embed any response to new challenges born from growing interdependencies within broader multilateral initiatives. In response to unforeseen exogenous forces, a core feature in China's North East Asian strategy has been to shift the centre of gravity of any cooperative effort away from North East Asia and towards other venues where it feels more at ease. Beijing's comfort level is dictated herein by both the relative power balances within a given venue, and its capacity to isolate and side-step objectionable or blatantly disruptive issues. North East Asian crises such as the North Korean nuclear issue's problematic re-emergence in '03; the Asian financial crisis such in '97; and even global upheavals such as the '07/08 financial meltdown, have all prompted China to advocate embedding North East Asian discussions within broader venues. As this drift towards 'embedding' is shared by all North East Asian actors, the sole source of controversy and main strategic stake within multilateral and regional calculations is the definition of the most appropriate forum.

Accordingly, China's North East Asian Neighbourhood policy is an ad hoc set of reactive policy initiatives born from a decades-old cyclical policy path wherein phases of engagement and denunciation succeed each other without threatening the underlying inertia of the sub-region. Furthermore, the main concern of China's North East Asian policy with regards to the emerging forms of Asian multilateral or regional cooperation is the relative importance given to the various existing venues.

A historical analysis of the developments fostered by China in its northern peripheries has isolated a deeply rooted distinction between both 'sides' of China's northern periphery. In contrast to the ENP's politically-dictated centripetal re-organizing logic, China's approach to its northern peripheries is far more centrifugal and respectful of specific historical experiences. As a result, it has developed quite distinct and relatively disconnected approaches to Central and North East Asia. Whereas China's approach to central Asia shares '89 as its foundational critical juncture with both the ENP and China's South East Asian efforts, the formative impact of the "*American unipolar moment*" on its emergence is an original feature. Just as with the ENP, the fact that

the neighbourhood policy in question is driven by unilateral concerns – be they endogenous in the case of the ENP and exogenous in China’s approach to Central Asia – the result is a rather rigid policy path which does not allow for much innovation or region–building. With regards to North East Asia, the absence of a Post–Cold War critical–juncture nearly fully negates any major Chinese region–building efforts towards North East Asia other than managerial ones aimed at preserving the status quo. Although stabilisation is a shared concern of the ENP and China’s North East Asian outlook, the profoundly conservative premises of the Chinese efforts are entirely different from the ENP’s transformational outlook (see Table 5).

Table 5: Historical Dimensions Compared: the ENP and China’s approach to NE and Central Asia

	Critical–Juncture & Catalysts	Policy–Paths	Drivers of Cooperation
ENP	Critical–Juncture '89 – Systemic Revolution Catalyst '04 – Enlargement	Policy Mechanisms inherited from enlargement processes	Endogenous Policy Debates
China's approach to Central Asia	Critical–Juncture '89 – Systemic Revolution Catalyst '01 – US invasion of Afghanistan	Classical Intergovernmental institutionalized Multilateralism	Exogenous Power encroachments
China's approach to NEA	Critical–Juncture None (Cyclical) Catalyst '97 – Asian Crisis '03 – Start of 6–Party Talks	Ad hoc, reactive, and more widely embedded efforts	Cyclical Inertia, <i>i.e. a shared willingness to maintain the status quo in spite of a rapidly and profoundly changing context</i>

In conclusion, this second comparison confirms that the ENP is again the more solidly rooted policy path, thus providing more predictability and principled policy positioning. As a transformative force ‘*written in stone*’ the ENP seems better equipped – although this is far from certain – to foster the predetermined policy goals. However, its institutionalized rigidities make it unresponsive and heavily unilateral. As a result the ENP is a poor hedge for broader strategic calculations. China’s northern initiatives are directly dictated by historical premises and systemic imperatives. Both the North East Asian and Central Asian dimensions of the CNP are specific expressions of core foreign policy goals. As a result, neither constitutes a foundation for the new Asian multilateralism or its corollary regionalism; rather, they are ‘facilitating variables’, oiling the wheels of change in a direction favourable to China’s overall geo–strategic goals.

4.2. Mutual Perceptions: From Another’s Cold–Shoulder to a Community’s Warm Embrace?

As mentioned above, the clearest reflection of China’s renewed geo–strategic multilateral drive towards inter–governmental alliances in its central Asian neighbourhood is the *Shanghai Cooperation Organisation (SCO)*. The SCO functions according to “*the principles of mutual trust, mutual benefit, equal rights, consultations, respect [...] conducted in accordance with the principles of non–alignment, non–targeting [...] and openness*”⁷⁷. Accordingly, China’s core models and taboos are an integral part of this strictly intergovernmental organization. The SCO is oriented towards a Chinese vision of “*he butong*” between sovereign states which implies cautious forms of “cooperation only where no differences exist” – i.e. *qiu tong cunyi*.

Even more undiluted than in the relationship with its South East Asian neighbourhood – where an ASEAN–way has influenced proceedings – China’s approach to its Central Asian proximity is one of straightforward unilateral projection of its domestic models and preferences. Socialisation, if present at all, remains heavily unidirectional. This fundamental inequality, in spite of the scrupulously guarded formal equality between sovereign states, is reflected in the SCO’s agenda which almost exclusively covers the concerns of the two main power–brokers: Russia and China. Most other members are clearly more concerned with ‘*band–wagoning*’ and ‘*hedging*’ on the back of their SCO membership, rather than with shaping the organization’s agenda⁷⁸.

As such the SCO reflects a shared tendency amongst all the BRICS–countries to seek to aggregate a ring of allied regional friends around them. This is not done necessarily with an eye on any specific problem–solving or community enhancing cooperation, but rather to isolate itself and its allies from supposedly undue external pressures⁷⁹.

China's efforts towards its Central Asian neighbourhood are therefore only secondarily a regional community–building exercise. They are first and foremost a balancing and insulation effort: a Westphalian sovereignty enhancing exercise. Logically, cooperation through the SCO is strategic rather than functional in nature. China seeks to bind its Central Asian Neighbourhood to its specific interests and models. In short, banking on growing strategic interdependencies, China's central Asian *neighbourhood policy* boasts more traits of a budding reactive balancing–alliance than of a functional sub–regional cooperation regime.

Conversely, not cross–border cooperation, but a classical understanding of the Westphalian state's pacification function stands at the centre of China's approach to North East Asia. Borders are not seen as bridging or buffering opportunities, but as methods of risk management through the insulation and enhanced certainty provided by the absolute "*illusion of*" sovereignty. This neighbourhood policy does not seek to complement the Westphalian state – neither through strategic balancing alliances nor through pragmatic functional regimes – instead it seeks to reaffirm its fundamental premise. Although China's North East Asian discourse is also centred on sovereignty enhancement, its more conservative and inward–looking concerns do not make it incompatible with wider region–building efforts. The North East Asia dynamics involving China have not underpinned any specific region–building effort, but have emerged as key arbiters regarding the feasibility and appropriateness of any multilateral regional scheme suggested elsewhere. Whereas China's constructive contribution of its own understanding of Asian multilateralism and regionalism is fed by its South East Asian neighbourhood policy, its North East Asian interactions crystallize its limitations and competing expressions. As a result, the core motor behind the current emerging Asian multilateralism and regionalism are push and pull dynamics between both of China's East Asian regional experiences (see Table 6).

Table 6: "Neighbourly" Models and Methods Associated with the ENP and China's NE and Central Asia

	Perception of the Outside	Geopolitical Models	Geostrategic Methods	Cooperative Dynamics	Relative Relations
ENP	Threat	Imperial	Limes/Marc	Consolidate	Unequal
	Opportunity	Neo–Medieval	Networked	Cooperate	Unequal
China's approach to Central Asia	Risk Containment	Westphalia	(Unilateralist) Modern Border	Insulate	(Qualified) Equal
China's approach to NEA	Risk Management	Westphalia	Modern Borders	Insulate	Equal

5. Conclusion

The ENP was ostensibly created as a single multilateral effort towards coalescing the EU's entire neighbourhood into a partner region defined by its proximity to, and dependence on, the EU. However, facts and policy practices have shown an EU far more interested in protecting itself from outside threats than in region-building. The ENP is therefore a policy rationalization and implementation effort, without any long term multilateral or regional preferences. More discerning in its approach, China has reproduced long-seated distinctions between its peripheries, adapting its approaches to each in accordance with its own strategic goals as a rising power. The EU, through its ENP, seems to have shrugged off the "burden of region-building" and even side-stepped its multilateralist ideals; whereas China's varying neighbourhoods have given it the opportunity to experiment and develop its own multilateralist principles, the community-building dimensions of which are embedded in the East Asian context. Whereas the EU's neighbourhood policies do appear as the more efficient immediate functional problem-solver, China's heterogenous experiences of multilateralism in its neighbourhood do offer a more strategic outlook towards multilateralism with domestic, regional and global implications. *Neighbourhood* for the EU is a laboratory for multilateral functional governance, whereas China's neighbourhoods have been its testing-grounds for a geo-strategic approach to multilateralism.

6. Endnotes

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Chapter 4

China and the Global Political Economy

Xinning Song and Weiping Huang

1. New Chinese Foreign Policy under the Hu Jintao Leadership

After end of the Cold War, Mr Deng Xiaoping, the Chinese leader, put forward the ‘24 Character Strategy’ as the basic principles for Chinese foreign policy, which included ‘Observe calmly; secure our position; cope with affairs calmly; hide our capacities and bide our time; be good at maintaining a low profile; and never claim leadership’ (冷静观察，稳住阵脚，沉着应付，韬光养晦，善于守拙，决不当头)[□]. Another 4 characters were added later, i.e. ‘do something’ (有所作为). The strategy has been also the guideline for Chinese foreign policy under the leadership of both Mr Jiang Zemin (1989–2002) and Mr Hu Jintao (2002–now).

Entering into the 21st Century, many Chinese government officials and scholars believed that China had a twenty-year ‘Strategic Opportunity’. This idea first appeared in the Political Report of the 16th National Congress of the Communist Party of China (CPC) in 2002 when Mr Hu Jintao replaced Mr Jiang Zemin as the Secretary General of the Party and then as the President of the State in 2003. The assumption behind the ‘Strategic Opportunity’ is that the first 20 years of the 21st Century is strategically important for Chinese political, economic and social development. Due to the possibility of a relatively peaceful international environment China needs to strengthen its effort for economic development and fulfils the strategic objective of establishing a well-off society¹.

In order to take advantage of this Strategic Opportunity, in October 2007 the 17th National Congress of the CPC highlighted certain new tendencies in Chinese foreign policy.

1.1. Strategic objectives of Chinese foreign policy and the harmonious world

The strategic objectives of Chinese foreign policy include three purposes: (1) Sharing opportunities for development; (2) Rising to challenges together; (3) Promoting the noble cause of peace and development of humanity. In order to reach these goals, the proposition of China is to join hands with the people of all countries and strive to build a harmonious world of lasting peace and common prosperity.

What is the real meaning of a harmonious world? There are two key words and five main elements. The two key words are *lasting peace*, and *common prosperity*. The five elements are: (1) Politically, all countries should respect each other and conduct consultations on an equal footing in a common endeavour to promote democracy in international relations. (2) Economically, they should cooperate with each other, draw on each other’s strengths and work together to advance economic globalization in the direction of balanced development, shared benefits and win-win progress. (3) Culturally, they should learn from each other in the spirit of seeking common ground while shelving differences, respect the diversity of the world and make joint efforts to advance human civilization. (4) In the area of security, they should trust each other, strengthen cooperation, and settle international disputes by peaceful means rather than by war and work together to safeguard peace and stability in the world. (5) On non-traditional security issues such as energy and climate change, they should assist

and cooperate with each other in conservation efforts to take good care of the Earth, the only home of human beings.

Although many Chinese commentators have emphasized that the Harmonious World is the initiative of Mr Hu Jintao, if we look at the official documents of the Communist Party of China, there are some pre-conditions for attaining the ideal harmonious world, which include upholding the tenets and principles of the United Nations Charter, observing international law and universally recognized norms of international relations, and promoting democracy, harmony, collaboration and win-win solutions in international relations. In other words, the Chinese concept of the harmonious world is based upon universal norms that come from the Western tradition rather than the ancient Chinese cultural tradition.

1.2. China's relationships with the outside world

In the 16th National Congress of the Communist Party of China in 2002, the Chinese leadership started to place the relationship with the developed countries, or Western countries, as its first priority. The ranking of Chinese foreign relations put developed countries first, neighbouring countries second, and third world countries or developing countries last. The 17th National Congress of the CPC kept the same ranking with different definitions or priorities.

Relationships with developed countries. In 2002 the emphasis was to improve and develop relations with the developed countries. Proceeding from the fundamental interests of the people of all countries concerned, we would broaden the converging points of common interests and properly settle differences on the basis of the Five Principles of Peaceful Coexistence, notwithstanding the differences in social system and ideology. In 2007 the focus was to continue to strengthen strategic dialogue, enhance mutual trust, deepen cooperation and properly manage differences to promote long-term, stable and sound development of bilateral relations. We can see that the Chinese leadership puts the relationship with developed countries as the most strategic one and would like to have a long-term, stable and sound bilateral relationship with them.

Relationships with neighbouring countries. In 2002, China would continue to cement our friendly ties with our neighbours and persist in building up a good-neighbourly relationship and partnership with them. We would step up regional cooperation and increase our exchanges and cooperation with our surrounding countries. In 2007, the emphasis was to follow the foreign policy of friendship and partnership, strengthen good-neighbourly relations and practical cooperation with them, and energetically engage in regional cooperation in order to jointly create a peaceful, stable regional environment featuring equality, mutual trust and win-win cooperation.

Relationships with developing countries. In 2002 what the Chinese leadership stressed was to enhance solidarity and cooperation with other developing countries, increase mutual understanding and trust and strengthen mutual help and support. We would enlarge the areas of cooperation and make it more fruitful. In 2007 China would like to continue to increase solidarity and cooperation with them, cement traditional friendship, expand practical cooperation, provide assistance to them as far as we are able, and uphold the legitimate demands and common interests of developing countries. The key words here are traditional friendship, practical cooperation, assistance as far as we are able.

To summarise, China upgrades its relationship with developed countries to the level of a strategic relationship, and pays more attention to pragmatic cooperation with its neighbours and other developing countries.

Within the Chinese foreign policy agenda, the position of two major countries is not very clear, i.e. Japan and Russia. Japan should be part of the developed countries, as well as neighbouring countries. Russia is not one of the developed countries, and only a neighbouring country.

According to this agenda, the United States and the EU as well as the EU member states are the most important partners for China, and Japan and Russia are next. Other neighbouring countries such as ASEAN and the South and North Koreas are third. Developing countries in Africa and Latin America are at the lowest level.

1.3. Keeping a low profile in international affairs

There were big debates on the issues of the 'peaceful rise' several years ago in China, especially in 2003. The major argument regarding the concept was if China should continue to keep a low profile or it should take a

more active role in global affairs. The Chinese leadership gave up the peaceful rise concept and changed it to the concept of peaceful development.

The 17th National Congress of the CPC emphasized very strongly that 'China will unswervingly follow the path of peaceful development. This is a strategic choice the Chinese government and people have made in light of the development trend of the times and their own fundamental interests'. And at the same time, the major contribution of China to regional and global development is 'through our own development, and effort in the areas where our interests meet with those of various parties'².

China's low profile diplomacy can be reflected by some very important changes in its foreign policy statement in the 17th Party Congress.

First, there is no mentioning of setting up a new international order, a slogan China started to use from the 1970s. There is even no mentioning of reforming the old international order, but only an emphasis on 'working to make the international order fairer and more equitable'³. It seems that this is the first time that the Chinese leadership clearly recognizes the legitimacy of the current international order in an official document.

Secondly, there is no mention in the report of the so-called comprehensive national capabilities and China as a great power in world affairs. There is continued emphasis on China still being a developing country. There is also no word regarding China as a responsible power. The emphasis is on China being part of the interdependent world, and that China would like to work with everybody in the world. There is a mention that China will continue to take an active part in multilateral affairs and assume its due international obligations. In comparison with the 16th Party Congress in 2002 when the CPC stated that 'we will continue to take an active part in multilateral diplomatic activities and play our role in the United Nations and other international or regional organizations'⁴, this is a more active stance.

1.4. Multilateralism and responsible power

Before 2000 what China always emphasized was multipolarity, which has been the official discourse for many years, rather than multilateralism. Some Chinese scholars started to challenge the concept of multipolarity in the late 1990s, advocating pluralism as its replacement, and arguing that the tendency in the post-cold war international system was non-polarity instead of multipolarity⁵. In July 2001, Chinese scholars discussed multilateralism and multilateral diplomacy in Beijing⁶. It was the first time that Chinese scholars looked at multilateralism from both theoretical and policy perspectives. The main Chinese understanding of multilateralism in early 2000s was very much the same as balance of powers and multipolarity. As some of them argued, multilateral diplomacy was the appropriate approach to the multi-polar world⁷.

The Chinese government started to change the discourse from multipolarity to multilateralism after 2003. Since then many Chinese leaders and governmental officials started to talk more about multilateralism, rather than multipolarity⁸. Multilateralism was firstly regarded as one of the most important areas of common ground between China and the European Union for constructing the EU-China strategic partnership⁹. Later, multilateralism, especially regional-multilateralism, became the new choice for China's foreign policy in general¹⁰. In April 2004 during the Foreign Ministerial Meeting of the Asia-Europe Meeting (ASEM) Mr Li Zhaoxing, the Chinese Foreign Minister, used 'effective multilateralism' officially for the first time in his speech¹¹. Several months later Mr Wang Yi, the Vice Minister of Foreign Affairs talked again about multilateralism in his speech at the 14th Ministerial Meeting of the Non-Aligned Movement, regarding it as 'the only choice to tackle globalization; and it is the tendency of the new era'. He also gave a new definition of multipolarity. 'The multipolarity we proposed is not that which contends for hegemony among great powers in history, but the harmonious co-existence and balanced development of the many forces in order to maintain the stability of the international community'¹².

As many people argued, the Chinese understanding of multilateralism is very much different from the European one¹³. For the Chinese, multilateralism is a kind of inter-governmental arrangement to deal with common issues. With the regime, every sovereign state is equal and the main principal is non-intervention in other's internal affairs. For China, multilateralism is more like a kind of diplomatic tool rather than a mechanism for international order. So the most popular concept in China is multilateral diplomacy¹⁴.

The Chinese always have big debates on China's role in world affairs. The official definition of China's position is China as a socialist and developing country. The outside world always mentions China as an emerging power or

even an emerging superpower. But most Chinese do not accept this definition. For many of them, China is still a regional power instead of a global power. China has been trying to be a normal member of the international community. But it has not reached that position entirely, because China is still regarded as an OTHER, similar to a rogue state, by many Western people and even governments. China is always put in the same list together with North Korea, Cuba, Iran and Iraq. One of the particular examples is that it is always not easy for PRC citizens to travel abroad due to visa restrictions by many Western countries.

Thus, the argument of the Chinese is that, if China is not regarded as a normal member of the international community by the Western states, why should it always be required to bear the obligations of a normal member? The Chinese government has mentioned many times that China would like to be a responsible country within the world community. The concept of stakeholder advocated by the Americans is also well accepted by Chinese officials and scholars. But many ordinary Chinese people do not care very much about this. What they care about is how China is treated by the outside world, especially by the Western countries, i.e. the United States and Europe.

The 17th Party Congress did not mention anything about China as a responsible power. The reasons could be two. Firstly, China has not regarded itself as a global power or even a POWER. In Chinese language 'power' has both positive and negative connotations. Secondly, China still believes that the peaceful, stable and sustainable development of China itself, economically, politically and socially, is the greatest contribution to the regional and global development. To be a responsible member of the international community, China should pay more attention to its own domestic affairs instead of external ones. Chinese foreign policy should serve China's domestic development. Because of this inward tendency of Chinese foreign policy, China focuses more on regional multilateral affairs rather than global ones.

2. Priorities in Chinese Foreign Policy

The Chinese strongly believe that foreign policy is the continuation of domestic politics and it must serve the national development strategy and domestic politics. The priorities of Chinese foreign policy can be divided into different levels such as domestic versus international, bilateralism versus multilateral, and regional versus global.

2.1. Domestic versus international

After 60 years of the People's Republic of China, especially the opening-up and reform in the last 30 years, China has achieved a great deal in economic development and external relations. But the most important domestic issue is still troublesome to Chinese Communist Party leaders, i.e. the political legitimacy of the Party.

Many Chinese believe that the major challenge to the Communist Party of China nowadays is the legitimacy of the ruling position of the CPC. In the first 40 years of the People's Republic of China, the basis of the legitimacy of the CPC was neither public participation nor social or economic welfare, but the charisma of personal leadership such as Mao Zedong and Deng Xiaoping, the ideology of Communism plus nationalism, and the centralized political system. After 30-year domestic reform and opening up to the outside world, the ideology of Communism has lost its base. Nationalism is still a force because of the Sino-US, Sino-Japanese and Sino-European disputes in various fields. But it is also a challenge to the current leadership. Along with the market economy system, decentralization has become the common demand from local levels. Mr Jiang Zemin came into power in very special circumstances. He had no choice but to follow the direction pursued by Mr Deng Xiaoping. His reputation as a Chinese leader is not so strong among ordinary Chinese people. Mr Hu Jintao was actually nominated by Mr Deng Xiaoping as the 4th generation of Communist leader.

Although the Chinese Communist leadership is facing a big challenge, most Chinese still believe that no other political forces can and should replace its ruling position because it was the Communist Party of China that started the process of reform and opening-up policy and has provided more economic benefits and a better living standard to Chinese people. This also means that the only legitimacy of the CPC is economic welfare. For the Communist Party of China, the only way to keep its ruling position is to keep the Chinese economy developing constantly.

For the Chinese leadership, foreign policy is determined by domestic politics and should serve domestic politics and economics. Because of the legitimacy problem of the Communist Party in China, political stability is regarded as the most important issue in China. But how to maintain political stability is the question: to strengthen the so-called 'People's Democratic Dictatorship', or go through economic development and economic welfare? The answer is the latter. Economic development is not only a matter of strengthening China's national capabilities, but is also a matter of maintaining the ruling position of the Communist Party in China. This is the most important domestic politics in China. The major task for Chinese foreign policy is then to pursue a peaceful international environment for China's economic development¹⁵.

2.2. Bilateralism versus multilateralism

Many countries pursued bilateralism or unilateralism as the main approach in their foreign policy for a long period of time after World War II, with the exception of the Western European countries. The special international circumstance giving rise to this was United States foreign policy after World War II, although the US was the major initiator of the global economic multilateral regimes. It was also US foreign policy that forced many countries to pursue either multilateralism or bilateralism in their regional foreign policy. In Asia, the United States put forward a bilateral approach by the establishment of bilateral military alliances with various individual Asian countries such as Japan, South Korea, Philippines, etc. In contrast, the United States put into practice a multilateral approach in Western Europe within the framework of the Marshall Plan and forced the Western European countries to work together as a group in order to receive the US assistance, even though the initial objective of the Plan was not to support European integration.

The Chinese Communist Party emphasized an independent foreign policy even before it came into power in 1949 because it did not want to rely too much upon the Communist Party of the Soviet Union. The People's Republic of China was forced to carry out a so-called 'lean to one side' foreign policy and it became the member of the Socialist Camp led by the Soviet Union because of the Korean War which began in 1950. The Socialist Camp and the Warsaw Pact Organization could be regarded as a multilateral arrangement among the Socialist countries in the 1950s and 1960s. It was also because of the bad experience with the Socialist Camp, where the multilateral approach was regarded by Chinese as a kind of hegemonic system that China finally broke with the Soviet Union, dropped out of the Socialist Camp and put into practice the so-called independent and self-determinate foreign policy. Both the United States and the Soviet Union were defined in terms of an hegemony, in a very negative way. From the late 1950s to the 1980s, China kept its posture of unilateralism and bilateralism in foreign relations, and strongly supported the non-alignment movement¹⁶. Only after 2003, China started to talk about multilateralism and looked upon it as one of the strategic tools to deal with international affairs, especially its neighbourhood policy.

Bilateralism was the traditional approach for China in dealing with its neighbours. One of the reasons was because China was worried about a multilateral arrangement being the tool of others to constrain China, as the United States and the Soviet Union did in the 1950s and 1960s. Another reason was that most of China's neighbours were allies of either the United States or the Soviet Union during the Cold War era. China had a strong sense of being threatened by neighbours that were influenced by the two hegemonic superpowers¹⁸.

After the cold war, China started to participate in the regional arrangements in the Asian Pacific such as Asia-Pacific Economic Cooperation (APEC) in 1991 and the ASEAN Regional Forum (ARF) in 1994. But the main dynamics of Chinese involvement was to use the regional platform to deal with bilateral issues and to counteract the influence of Western sanctions after the 1989 event. A good example was the importance of the bilateral meetings with the major counterparts in the region, especially the United States and Japan, during the annual APEC informal Summit. These meetings were more important for China than any regional agenda within the APEC framework¹⁹.

China started its new 'Good Neighbourhood Policy' from the early 1990s. The main content of the policy was 'to act appropriately towards neighbours and to be a partner with neighbours'²⁰. Since the second half of the 1990s, Asian regional cooperation has developed smoothly on the one hand, and the sensation of the 'China Threat' on the part of China's neighbours increased on the other hand. China's economic and military capabilities were regarded as the major reasons for this perception. China's traditional way of dealing with neighbours faced great challenges because it became increasingly difficult for the Chinese authorities to deal with all its neighbours separately. It is easy for China 'to act appropriately towards' its neighbours. But it is very difficult for China 'to

be a partner with' all its neighbours separately. The best way is to have a partnership with all its neighbours through certain regional–multilateral mechanisms.

In October 2003 Mr Wen Jiabao, the Chinese Premier, put forward a new conception of China's neighbourhood policy, i.e. 'to build an amicable, tranquil and prosperous neighbourhood in the region'²¹. According to Mr Wen, to build an amicable neighbourhood means benevolence, good neighbourliness and harmony; to build a tranquil neighbourhood is to actively maintain peace and stability in the region; to build a prosperous neighbourhood is to step up mutually beneficial cooperation with the neighbouring countries, deepen regional and sub–regional cooperation, and vigorously facilitate economic integration in the region, thus achieving common development with other Asian countries.

The new strategy is to move away from the traditional 'bilateral plus regional' approach, i.e. using a regional platform just to deal with bilateral relations, to a new 'regional–multilateral plus bilateral' approach, i.e. to engage in more regional cooperation and work with neighbouring countries together within the regional–multilateral arrangement in order to resolve bilateral problems. Bilateral issues, especially border issues with different neighbours, could be easily resolved or put on ice at the same time assumed by some Chinese scholars.

China's regional–multilateral approach to deal with regional issues and neighbouring countries can be regarded as part of China's neighbourhood policy, as well as its global strategy. In terms of China's neighbourhood policy, bilateralism is not enough to safeguard China's national security and economic interests. In terms of global strategy, China would like to play a more important role in global affairs with the condition of a stable and secure regional environment.

But China's regional–multilateral approach or efforts to engage in regional cooperation is not to pursue an EU–style regional integration. Many scholars have argued that there has been no real regional integration in Asia because 'integration' has a very special meaning and is strongly related to institutionalization and legalization²². The dynamics of China's regional approach include two challenges. The first is to resolve the bilateral problems with the neighbours. As mentioned, it is very difficult for China to be partner with its neighbours separately. The main objective is to keep a good relationship with all the neighbours through different regional arrangement such as ASEAN plus one, the Shanghai Cooperation Organization, East Asia Summit, and Northeast Asia–3 Summit. The second is that, in order to play a more active role in global affairs, China needs a stable, prosperous and secure regional environment.

China's multilateralist strategy is mainly for regional affairs rather than global affairs. Globally, the Chinese focus on multilateralism relates to the United Nations and global economic institutions such as the WTO and IMF. With regard to the responsible power argument, China pays more attention to the bilateral relationship with the major powers in the world, rather than global multilateral regimes, because the IMF and World Bank are still regarded as Western–dominated regimes by many Chinese. Even in the United Nations, for China, the relationship with the other four permanent members of the Security Council is always the priority.

Four more principles of Chinese diplomacy were established after 2002, i.e. 'great power as the key, periphery as the core, developing world as the foundation, multilateralism as the stage' (大国是关键, 周边是首要, 发展中国家是基础, 多边是舞台). This shows that China still pays more attention to the bilateral relationship with the major powers. Some people have also argued that the Chinese multilateralist strategy is actually a selective multilateralism²³.

2.3. Regional versus global

Most Chinese still regard China as a regional power rather than a global power, or regional power with the characteristics of the global power. There are several reasons for this. Firstly, China's economic development level is still very weak and GDP per capita is at a very low level in international terms, although total GDP has reached number two in the world. Secondly, China's economy is very much dependent upon the global market, especially the Western economies. Thirdly, and most importantly, China's national interests, especially its national security interests, are more regional than global.

When China negotiates with other major powers such as the United States, the EU, Russia and Japan, it always talks about mutual respect for each other's vital interests. The vital interests of China are related to sovereignty, territorial integrity and national security, with issues such as Taiwan, Tibet, Xinjiang, and the North Korean nuclear

programme. All of these are regional. Although the Middle East and Africa are becoming increasingly important for China, they have not been priority issues for China, and probably will not become so in the near future.

Economically, the major economic partners of China are three: the United States, the EU and East Asia. The EU has been the first trade partner of China since 2004 and has always been the most important provider of technology. The United States ranks as the second. But actually, China has more trade with East Asia (Northeast Asia and Southeast Asia) than the EU and the US together. In 2008, China's trade with East Asia was 1016.90 billion US\$ (39.70% of China's total) and trade with the EU-27 was 425.57 billion US\$ (16.61% of China's total) and 333.74 billion US\$ with the United States (13.03% of China's total). In 2010 with a significant recovery from 2009, China's trade with East Asia was 1173.66 billion US\$ (39.48% of the total) and 479.71 billion US\$ with the EU (16.14% of the total), 385.34 billion US\$ with the US (12.96% of the total)²³. Some people have even argued that if one takes APEC as a whole, it will account for more than 70% of China's total foreign trade.

Table 1. China's Foreign Trade in 2008 (billion of US\$)

	Total trade	%	Export	%	Import	%
China	2561.632	100%	1428.546	100%	1133.086	100%
Asia	1365.952	53.32%	663.295	46.43%	702.657	62.01%
Japan	266.785	10.41%	116.134	8.13%	150.651	13.30%
South Korea	186.113	7.27%	73.951	5.18%	112.162	9.90%
Hong Kong	203.666	7.95%	190.743	13.35%	12.923	1.14%
Taiwan	129.217	5.04%	25.878	1.81%	103.340	9.12%
ASEAN	231.117	9.02%	114.142	7.99%	116.974	10.32%
East Asia	1016.898	39.70%	520.848	36.46%	496.050	43.78%
EU-27	425.577	16.61%	292.878	20.50%	132.699	11.71%
USA	333.738	13.03%	252.297	17.66%	81.440	7.19%
Canada	34.520	1.35%	21.789	1.53%	12.731	1.12%

Table 2. China's Foreign Trade in 2009 (billion of US\$)

	Total trade	%	Export	%	Import	%
China	2207.219	100%	1201.663	100%	1005.555	100%
Asia	1172.049	53.10%	568.597	47.32%	603.452	60.01%
Japan	228.848	10.37%	97.911	8.15%	130.938	13.02%
South Korea	156.232	7.08%	53.68	4.47%	102.552	10.20%
Hong Kong	174.945	7.93%	166.233	13.83%	8.712	0.87%
Taiwan	106.228	4.81%	20.505	1.71%	85.723	8.52%
ASEAN	213.011	9.65%	106.297	8.85%	106.714	10.61%
East Asia	879.264	39.84%	444.626	37.00%	434.639	43.22%
EU-27	364.042	16.49%	236.284	19.66%	127.758	12.71%
USA	298.259	13.51%	220.816	18.38%	77.443	7.70%
Canada	29.701	1.35%	17.675	1.47%	12.026	1.20%

Resources: General Administration of Customs of the People's Republic of China,

www.ChinaCustomsStat.com.

Table 3. China's Foreign Trade in 2010 (billion of US\$)

	Total trade	%	Export	%	Import	%
China	2972.76	100%	1577.93	100%	1394.83	100%
Asia	1566.68	52.70%	732.07	46.39%	834.61	59.84%
Japan	297.77	10.02%	121.06	7.67%	176.71	12.67%
South Korea	207.17	6.97%	68.77	4.36%	138.4	9.92%
Hong Kong	230.58	7.76%	218.32	13.84%	12.26	0.88%
Taiwan	145.37	4.89%	29.68	1.88%	115.69	8.29%
ASEAN	292.78	9.85%	138.21	8.76%	154.57	11.08%
East Asia	1173.67	39.48%	576.04	36.51%	597.63	42.85%
EU-27	479.71	16.14%	311.23	19.72%	168.48	12.08%
USA	385.34	12.96%	283.30	17.95%	102.04	7.32%
Canada	37.11	1.25%	22.22	1.41%	14.89	1.07%

Resources: General Administration of Customs of the People's Republic of China,
www.chinacustomsstat.com/asp/1/NewData/Stat_Class.aspx?state=3&t=2&guid=4647

3. China's Economic Development Strategy

Between 1947 and 1948, just before founding of the new Republic, China could only produce 1/87th of America's steel production and 1/8th of Japan's; 1/9th of American's coal production, but the same as Japan's; and 1/35th of America's electricity production and 1/6th of that in Japan. Since 1998, China has already risen to first in steel, coal, cement, cloth, TV sets, motorcycles, tape recorders, washing machines, grain, cotton, meat, seafood, egg production. Power and crude oil production are already ranked 2nd and 4th. The production capacity for TV sets, refrigerators and washing machines accounts for the 1/3rd of the worldwide total today. There seems to be no doubt that the industrial production of China today ranks between 4th and 3rd worldwide.

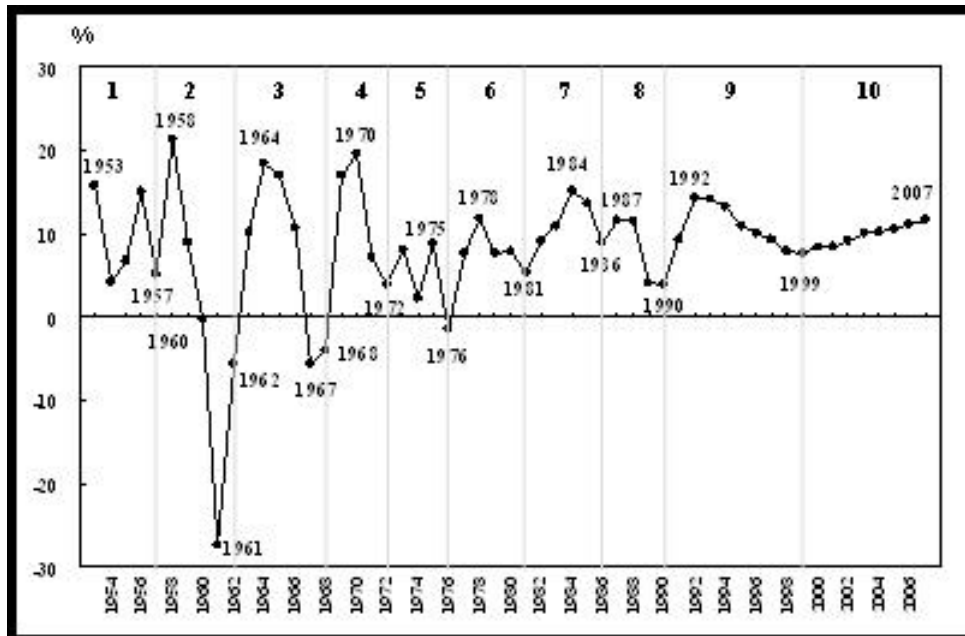
The economic crisis of 2008–2009 meant all world slowed down in terms of development and, in that context, China took over Japan in 2010 in GDP. Compared with the USA, Japan and EU, China's miracle of development in the region might be not so smooth looking forward, not because of the effects of the financial crisis, but due to China's so-called un-sustainable development model – with a clear business cycle (see Figure 1), serious pollution, low efficiency in use of natural resources, a big gap in income distribution, no self-sufficient supply of high tech, serious trade disputes with partners, real estate and stock market bubbles, and so on, as well as a slowing down of the reform of the political system.

How to promote sustainable development, and what should be the main route for China's development in the near future, are the issues that should be kept in mind. A group of indicators is given below to make it clear.

In the hope that China will be a real partner of the members of the global village in the world economy, China has to meet certain requirements or criteria in order to be one of the leading economies in the World, to reach the power that it needs to be able to take responsibility within world economy.

1) It has to be a top economic power in the world, which means having a large GDP both in absolute terms and per capita (in 2010, the GDP of China reached \$5880 billion, although the GDP per capita was only \$4200 and far from the developed ones).

Figure 1. Growth rate in China 1953-2007



2) With the largest population in the world, China needs a large proportion of highly qualified people, not only workforce, in the total population. That means that the cultural–educational level of people in China should be much higher than that of today in order to modernize the country.

3) China requires an advanced industrial structure, especially leading sectors in important industries (but without a dual structure in society, i.e. the existence of rich and poor, advancement and backwardness in the economy at the same time). It has also to be progressing toward the future consolidating of the post – industrialized or so–called information society.

4) A market oriented or market–driven economic structure and rational allocation of different resources (production resources) with high economic efficiency, involving very significant technical and institutional progress in the economy is another challenge.

5) Another key factor is a huge market capacity, which means being able to absorb a large amount of domestic and foreign economic output, having the power to push development by greater domestic demand.

6) Effective power of control is needed too, especially the power of control over the flows of resources including high–tech equipment, workforce (qualified workforce), capital funds, information and other natural or non–natural resources.

7) One more request is the strengthening of a reasonable social structure, stable social system and pattern. Social life should be institutionalized and with a highly social civilization.

8) Finally, there should be a very significant contribution to, and interest in, world economic affairs, with a great willingness to participate in worldwide economic and political affairs.

China wishes to meet the requirements mentioned above within the next 30 – 50 years, and become one of the rich countries in the world. In this case China would be friend of all the economies and would lay the foundation for exchange with the rest of the world including both rich and poor. To judge by economic history, we consider to be certain that China will reach the goal of development by the middle of this century.

Although China is significantly stronger than before, with \$4200 per capita in 2010, and has been able to meet the UN Millennium Development Goals (MDG) of halving poverty and universal primary education, ahead of schedule, it is still one of the largest developing economies in the World, and has had to fight serious poverty. After more than 30 years of reform and opening up and rapid economic development, China’s impoverished

rural population has fallen from 250 million in 1978 to 21.48 million, and the rate of poverty has dropped from the original 30.7 per cent to 2.3 per cent (see Figures 2 and 3). The nine-year compulsory education population coverage has also been reached at 98%

Figure 2. The change in China's rural poor (1978-2005)

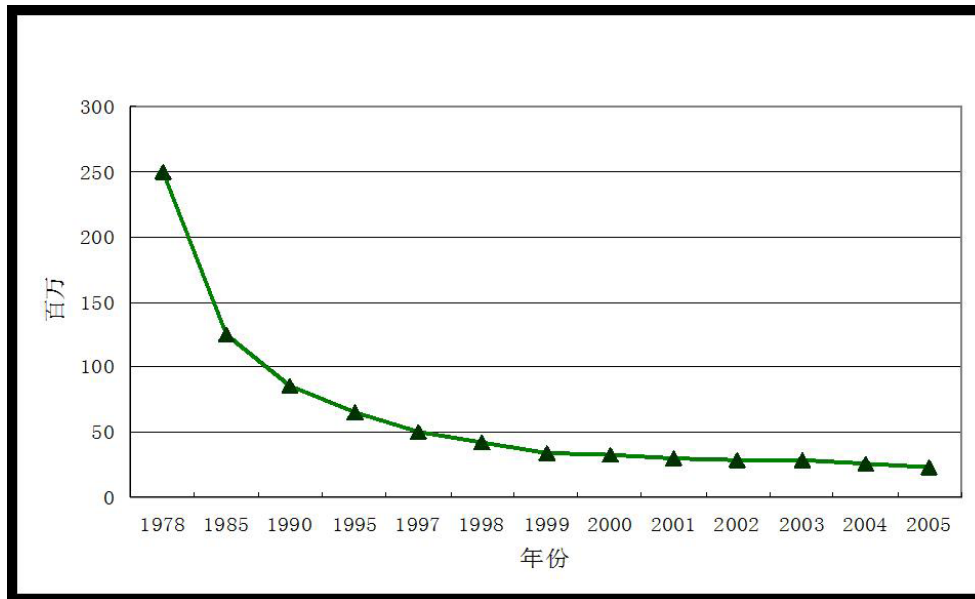
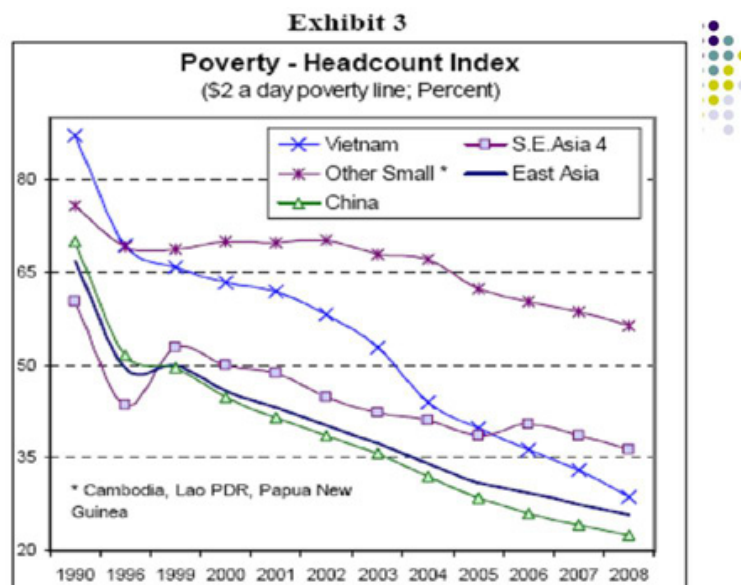


Figure 3. Poverty headcount index



To fight poverty in China, China should establish an anti-poverty policy in the near future that comprises: 1) The establishment of a standard development poverty line, the long-term goal of poverty alleviation. 2) The setting up of a rational system of credit and poverty alleviation with financial sector participation. 3) The planning and improvement of the urban and rural social security system. 4) The promotion of the process of urbanization, and provision of social security and public services to the floating population in cities. 5) The provision of more equal opportunities in education. 6) The expansion of rural labourers' occupational and skills training and labour export. 7) The establishment of a rational public finance poverty alleviation mechanism, to strengthen the management of the government when dealing with poverty.

Meanwhile, in the next decade, China's redistribution of income should be reformed. In that sense the most efficient way of increasing the income of the poor is to promote a movement of labour from traditional industries into modern industries. Statistics show that about 130 million people from the countryside have sought jobs in the country's urban areas since the late 1980s. Most of them work as construction workers, security guards and waiters, where they encounter low and often delayed pay, long working hours, poor safety conditions, lack of social security, inadequate schooling for their children and substandard living conditions.

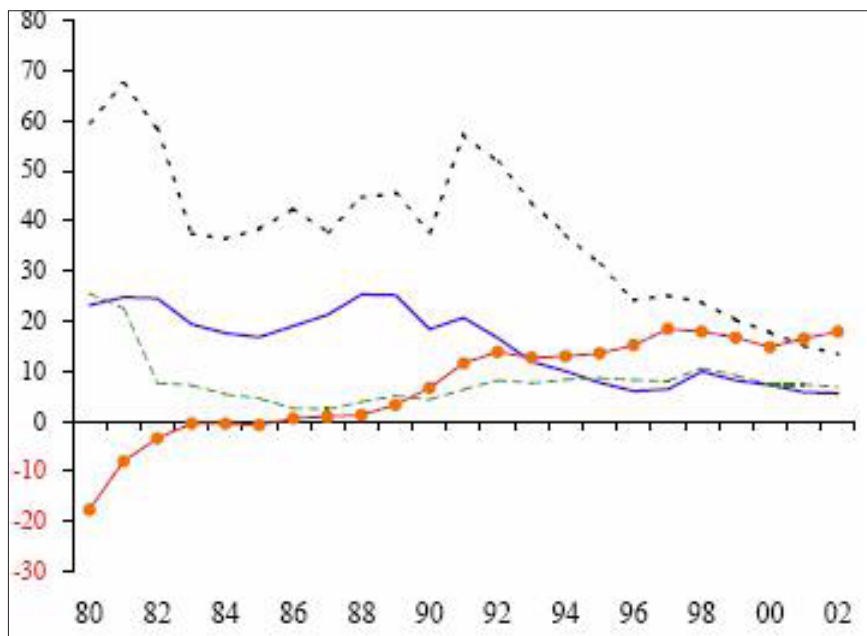
4. Sino-US and Sino-EU Economic and Trade Relations

China's external trade in 1978 was ranked 32nd in the world. It reached the 11th position in 1995, subsequently the 10th in 1998, the 9th in 2000 and finally the 2nd in 2009, which is really great progress in historic terms achieved through the modernization of its economy.

External trade also contributed greatly to the increase of the foreign exchange reserve, which was USD 19.44 billion in 1992, USD 51.62 billion in 1994, growing up to USD 144.9 billion in 1998 and USD 2847 billion in 2010. Meanwhile China's degree of dependence upon external trade increased year by year, which shows that China is deeply involved with and integrated into the world economy, and that the development of China is closely associated with global economic changes. Within economic globalization, China's progress has been impressive.

As we all know, every family in the US is able to buy Chinese products that are reasonable in price and good quality. Both US enterprises and all commercial activities have benefited a lot from Chinese trade. The past 20 years have seen a faster growth period than ever for Sino-US trade. According to China's statistics, total trade with the US has reached US\$385.3 billion in 2010 at an annual growth rate of 29.2 percent, with China's exports to the US increasing by 28.3 percent to US\$283.3 billion. Imports from the US grew by 31.7 percent to US\$102 billion²⁴. Accordingly, the strong growth has made the US China's second largest trade partner. Meanwhile, US investment in China has also surged in recent years. There are over 58 362 US-invested companies operating in China, with US\$ 63 billion capital investment by 2008. Based on the US Census Bureau's statistics, China was the second largest import and 3rd largest export trade partner of the US²⁵.

Figure 4. Percentage of Trade Deficit in US Total; red is China's contribution, black is Japan's, blue is the Four Tigers' and green is ASEAN's



In view of the trade relationship between the two countries, there is a serious trade imbalance between China and the US, which, in fact, has soared year after year to a new record. In accordance with China's data, the US trade deficit with China reached US\$170.1 billion in 2008 (it was US\$181.3 billion in 2010), while it was more than US\$266.3 billion based on US statistics in 2008. All in all, China is now the biggest contributor to the US trade deficit, and 100% of total China's trade surplus comes from the US in 2010. In 2010, China is the US's 3rd ranked export partner and first ranked import partner, according to US Department of Commerce. Although there are conflicts in the two countries' bilateral economic and trade activities, somehow trade has continuously developed despite the disputes.

The Sino-EU trade relation developed rapidly. Today, EU is the largest trade partner and the first exporting market for China. China is the 3rd largest export market for the EU (see Table 3).

Besides the figures evolution, trade disputes between China and the US and the EU, apart from the trade surplus, have always been a long-standing issue. They were becoming more and more important before China's WTO accession, and even affected China's accession process. This is shown by the requests made and opinions expressed by the US and EU during the current trade dispute negotiations.

Import Policy

China started to lower import tariffs before its entry into the WTO, and reached the goal set during accession to WTO. The US and the EU still complained that China restricts imports by a variety of means, including prohibitively high tariffs and domestic tax on imported products, non-tariff-related measures, restrictions on Chinese enterprises' import licenses and other trade barriers. For example: for some motor vehicles, the tariff could be as high as 25 percent. In addition, the tariff might vary for the same product depending on places of entry.

Sometimes additional domestic tariffs might be added, or some local restrictive rules might apply. Moreover, imports may also be subject to value-added tax and other duties. The current value-added tax system (VAT), usually at 13 or 17 percent, was also complained about by US and EU trade partners because if a product was subject to a 10 percent import tariff and a further 17 percent VAT, the total consumption tax would be at a rate in excess of 27 percent.

As to China's non-tariff trade barriers, there are also some issues to resolve. For example, recent dispute on the rare earths metals. For some other products, after permission has been granted by other administrations for import, Ministry of Commerce still has the right to decide whether a licence should be issued.

Transparency

Although in recent year China's trading system has become significantly more transparent, the US and EU trade partners suggested that they sometimes encountered difficulties in identifying which rules and regulations apply to their operations in China.

Issue of Standards

The US and EU trade partners complain about the problems of the standards system in China, which include a lack of transparency, difficulty in determining appropriate standards, use of different standards on imports from different countries and domestic goods. For example, US traders are not sure which Chinese standards apply to their goods. Sometimes a particular good of the same type imported from the US and from the EU are inspected in accordance with different standards when they are imported to China. American trade partners also complain that China's sanitary and phytosanitary import quarantine standards are often overly strict, unevenly applied, not the same as those used for domestic trade and not backed up by modern laboratory techniques.²⁶

Government Procurement

The US and EU complain that government procurement practices are unclear and there is a lack of transparency. Although China committed to announcing all related laws and regulations, it did not publish any specific rules and regulations on government procurement practices before its accession to the WTO. Moreover, competitive bids for tenders were not allowed for most government procurements in China for the governmental investment during the financial crisis in 2008-2009.

Export Subsidies

The US complains that although the Chinese government claims that direct financial subsidies on all exports including agricultural goods had ended on 1 January 1991, Chinese exporters could still benefit from loan policies (non-commercial terms loan), export tax rebate (rebate on value-added tax), preferential tax policies (reduced income taxes), and preferential energy and raw material, as well as land supply policies. The US partner treats all these as discriminatory measures in trade, which today contributes most of the trade disputes between China and US.

Barriers to Service Industries

To the US and EU, China's service industry market is so closed that the Chinese government only allows foreign services providers to operate under selective licences. This is reflected in restrictions to foreign enterprises' investments and operations in service industries in China. Lack of transparency in administrative procedures limits the exports of foreign companies' services and investments to China. Service trade opportunities, particularly those in financial services, telecommunications, audiovisual, transportation, distribution, professional services, legal services, accounting services, tourism, and so forth, have been affected by a variety of restrictions. Recently, in 2010, a dispute arose relating to credit card issuing by the two sides, for example. The US traders think that obstacles such as labour employment, representative office establishment and joint-venture requirements make it very difficult for them to access China's market.

Investment Barriers

Although China's official policy welcomes foreign investment, US and EU investors consider that the Chinese government has imposed investment barriers and control on foreign investment that could channel it to the areas that China's economic development special needs. China encourages foreign investment in priority infrastructure sectors such as agriculture and high-tech sectors. On the other hand, it restricts or even prohibits it in sectors where China wants to protect local industries. In addition, China bans investment in certain industries citing 'national security interest', and forces overseas firms into joint venture arrangements, or insists on technology transfer from foreign companies.

Other Complains

The US and EU complain that the following WTO requests are not fully carried out in order to deal with the issues mentioned:

Uniform Administration. In China there are four different levels of authorities from central government to township, all with diverse laws, regulations, rules, directives, policies, standards, and so forth. All these criteria affect trade in goods, services, trade-related aspects of intellectual property rights or the control of foreign exchange.

Non-discrimination. Foreign individuals and enterprises and foreign funded enterprises should be no less favoured than other individual and enterprises in respect of goods, service and other trade business either at nationwide or sub-nation level.

Foreign Exchange Control. China accepted Article VIII of the IMF's Articles of Agreement, which means the openness of free foreign exchange in the Current Account of the Balance of Payments, but today the pressure on the Capital Account is growing.

5. Exchange of RMB to US Dollar: Manipulated?

The financial crisis in the US and other developed countries was the most significant event in the world economy during the period 2008–2009. This crisis adjusted the pattern and structure of the world economy and made financial issues headline news everywhere in the world, and have strong influences to the end of the first decade and the beginning of the second decade of the 21st Century. During the crisis, caused by the economic difficulties, the currencies in various countries were seriously devaluated, for example, the Indonesian Rupiah, Thailand Baht and Korean Won, and some of the economies in the world suffered negative growth in 2009.

In such a situation, China was almost the only economy in the world to be free from the shock because of its prudential and gradual opening of finance to the rest of the world.

Since China is one of the largest and most important economies in the world, its role in bringing stability to the international economic situation during the crisis has been also very important. In this regard there are many different comments and ideas regarding China's roles in diverse ways. The most popular two are set out here.

The first one is whether the Renminbi (RMB), the China's Currency, should be appreciated or not, under pressure from other economies to revalue. In our opinion, in the short and middle term that there is no reason for the RMB, to be revaluated, and in the long run, there is no reason not to retain flexibility, and valued by the market power for the RMB, taking into account development and the changing world economy.

The second issue is whether or not China should pursue some new and different policies in coping with the difficult domestic economic performance affected by the world financial and economic crisis in 2010. We think that the Chinese Government has taken some positive steps in terms of fiscal expenditure policy to increase domestic consumption in order to deal with the effect of a drop in exports, although China's export performance is quite impressive worldwide. There also must be a slowdown in investment increase to avoid over-heating the economy.

In any case, this is a controversial issue. Some economists suggest that an appreciation of the RMB would not hurt China's trade, because this would benefit from a decrease in the cost of imports and in the debt service of China? On the other hand, some other economists think that with the appreciation of the Chinese currency, China's economy would be hurt by a reduction in exports records, and that this could lead to a new financial crisis that would once again hit the world economy. With China insisting on non-appreciation of the currency, some economists of the world approve this policy but also believe that it will adversely affect Chinese economic development. China should consequently pursue some new policies to cope with the problem.

The following are some relevant points concerning the discussion about the RMB exchange rate:

1. From the analysis of the supply and demand of foreign exchange in the Chinese market, the RMB has a stable basis.
2. There is some possibility of the double-dip financial crisis with unclear effects and results for China and the world economy.
3. Currently the exchange rate of the RMB is set by roughly pegging it with the US dollar with the dynamic of the market, an artificial intervention which will produce the result of RMB appreciation in short term, but in the long run, the strength of the market power would adjust the rate, like in November 2011, the non-deliverable forward DNF of RMB depreciated for 10 days
4. A change of rate (appreciation or depreciation) of the RMB will be matched with the general direction of economic development, and reflecting the need of economic development of China first, with only secondary consideration of the effect of depreciation or appreciation on other economies.

A depreciation of other economies' currencies would put pressure on China's exports, but the pressure would be far less than the shrinkage of import demand caused by the financial crisis. China's recent policy alternatives will help in promoting imports, and with the recovery of economic growth in the world, China's exports would soar again in the future.

Trade competition is a comprehensive term which is based on different factors and elements; despite the competitiveness of products from other economies being increased by depreciation, it is not so easy to drive out Chinese products from their traditional market, especially from the developed market. The reasons for this are:

- 1) Depreciation of other economies' currencies during the crisis was forced, had to be and as the result of financial crisis, which would be different from a devaluation as a policy instrument to promote exports.
- 2) With the enclave feature, some parts of the production chain are a part of the overall system of multinational corporations (MNCs), and depreciation would not make MNCs redesign their strategy and shift more production out of China.

3) Most of the comparative advantage of China is due to economy of scale and reasonable labour costs, which could not be replaced in a short run by other economies.

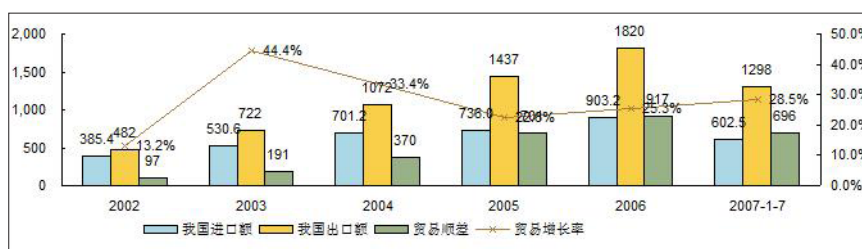
The financial crisis combined with the changing situation of world production have had a greater impact than domestic demand in China in recent years, and the uncertainty of the effects of the crisis has had a negative effect on the strategy of economic growth of China recently. The Chinese government has used both monetary and fiscal policy to cope with the economic difficulties, by increasing domestic demand while maintaining the increase in exports.

With all these fiscal and monetary measures taken by the Chinese government, plus all issues of authorities' bonds in recent years, the percentage of the Chinese fiscal deficit in terms of GDP and the country's debt burden will increase but they will still be lower than those existing in most of the economies in the world (3% of annual GDP and less than 50% of annual GDP, respectively, are acceptable). By using expansionary monetary and fiscal policy (commonly used by other economies also) China hopes to avoid a more seriously negative impact on economic development, and reach the economic growth rate target. Obviously, the result of monetary (including appreciation or depreciation of the RMB) and fiscal policy might be revealed after a time lag of several months or years; in the meantime, the Chinese government is paying much attention to the effect of the acceleration of investment and the crowding-out effect to avoid the negative impact of the bystander effect of fiscal policy, such as inflation in the future. The Chinese also hope that the all the economies in the world will recover soon, and consider that they have made a contribution to the world wealth by maintaining or even revaluating the stable exchange rate of the RMB, although this may have adversely affected Chinese economic development in some aspects. When worldwide recovery arrives, China will have no pressure to adjust the exchange rate of the RMB independently of the dynamic of monetary market in China and leave the pegging system behind.

Avoiding a US-China currency war: the need for rational calculation to avoid labelling China as 'a currency manipulator'.

Since July 2005, China's RMB has been revalued by 34 per cent. But this has neither significantly improved the US trade deficit, nor reduced China's trade surplus. Merely the prospect of a trade war, or a currency or exchange rate war, between the world's two largest economies would further delay the recovery of the world economy.

Figure 4. Percentage of Trade Deficit in US Total; red is China's contribution, black is Japan's, blue is the Four Tigers' and green is ASEAN's



Does China manipulate the RMB exchange rate? 'Yes' is the answer most widely accepted in the developed economies, but the basis for this is common sense, whereas the legal basis for this argument is unclear. What China adopted was fixed exchange rate policy in 1997-2005, a managed floating system in 2005-2008 and a soft pegging after August 2008. True, the People's Bank of China intervenes in the foreign exchange markets by purchasing US Dollars in order to maintain a stable exchange rate for the RMB. But can this be considered as 'currency manipulation'? A fixed exchange rate was the dominant regime under the Bretton Woods System (BWS), when the US Dollar was pegged to gold and all other currencies were pegged to the US Dollar. After President Nixon de-linked the USD from gold in 1971, the IMF started to encourage more flexible exchange rates from 1973. But the IMF never introduced any rules prohibiting any country adopting a fixed exchange rate. There are three official exchange rate systems accepted by the IMF and its member countries: fixed, floating and, in-between, pegging. For example, in Asia, most economies use the pegging: Hong Kong has a currency board arrangement and Singapore has a crawling peg. Neither the US nor the IMF appears to have any problem with these two economies.

A revaluation of the RMB would not help rebalance the global economy. The reality is, as China's Premier Wen Jiabao pointed out, that during 2005–2008, the RMB appreciated by 21 % against the US Dollar and by 16 % in real effective terms. But China's current account surpluses rose from 3.5 % of GDP in 2004 to 10.8 % in 2007, before moderating to 9.6 % of GDP in 2008 due to the global recession. In March 2010, China suddenly recorded a trade deficit of \$7.2 billion, despite the continuation of the RMB's soft peg to US Dollar. It is unlikely that further RMB appreciation, as demanded by some US congress representatives and some famous scholars such as Prof. Paul Krugman, can basically change China's status as 'factory of the world' and substantially boost American exports by doubling volume in 5 years as US President Obama hoped.

Goods that are 'Made in China' actually involve a collective division of labour chain across East Asian economies. In the past two decades, East Asian economies including Japan, South Korea, Taiwan, Hong Kong and Singapore have invested and moved their assembly lines into mainland China to take advantage of its cheap labour and land costs; parts and modules come from ASEAN economies and are assembled in mainland China; and exports thereof continue to be targeted at the US and EU market. As a result, these economies have greatly reduced their trade surplus with the US and EU, while increasing the surplus with China, and China is perceived as having the largest trade surplus.

The trade deficit also creates jobs. We can see this from the following case study by the National Board of Trade, Sweden²⁸.

A Dutch intermediary company is processing 95% of its sales of women's shoes in China. Value list for a pair of woman shoes:

1. Pre-manufacturing in EU (R&D: Euro 0.9, production and quality control: Euro 0.05);
2. Manufacturing process in China (Raw material: Euro 2.18, labour cost: Euro 0.93, Shipment: Euro 0.46, Insurance: Euro 0.04; Other costs -electronic power, water, etc: Euro 0.44, Profit: Euro 0.37);
3. Post manufacturing in EU (Tariff: Euro 0.35, Logistics: Euro 0.22, Retail: Euro 0.67). Retail price: Euro 19.95 (in EU).

Cost in EU:

$0.9+0.05=\text{Euro } 0.95;$

$2.18+0.93+0.44+0.37+0.46+0.04=\text{Euro } 4.42$

$0.35+0.22+0.67=\text{Euro } 1.24$

Total: Euro 6.61 (Wholesale price: Euro 6.65)

Value in China: $0.93+0.44+0.37=\text{Euro } 1.74$

Value in EU: $19.95-1.74= \text{Euro } 18.21$

(Raw material imported from EU)

That is, Euro 18.21 remains in the EU. The trade deficit is the differential of the prices between China and EU, which could be considered as the GDP of the EU, and each unit of GDP could create certain jobs, which is common sense.

The conclusion by the author is: 'We found that, even for a low price shoe, EU value added is above 50 %. For the medium price range EU value added can reach almost 70% and for up-market shoes, with high design and marketing costs, the EU value added can surpass 80%. This means that a shoe manufactured in China still can be regarded as a "European shoe"'²⁹.

To avoid a trade and currency war, some suggestions have been made, for example, by Prof. Ronald I. McKinnon who pointed out: 'So here we have the makings of a deal. China agrees to a one-off modest appreciation of the RMB while continuing to reduce its net saving surplus (trade) by increasing consumption. The US agrees to the People's Bank of China stabilising the Yuan-dollar rate indefinitely while working on reducing America's huge net saving (trade) deficit. Both sides agree to stop the (incipient) trade war which has seen them imposing, or threatening to impose, tariffs or other restrictions on the other's goods' ³⁰.

The suggestion of this author is: if the economic authorities cannot reach common agreement in relation to the RMB-US Dollar exchange rate, the best way to resolve this issue is to organize a team from the two sides, and allow the experts from the IMF and the World Bank to attend, and then to calculate the real value of the US Dollar and the RMB, and work out a central exchange rate accepted by two sides. The result of this teamwork would be the basis for any future discussion about the economic relation between China and US, given that, it is clear that any RMB exchange rate agreement is not just a domestic issue for China. As two of the largest economies in the world, any change to the US Dollar and China's currency would have an impact on the world economy. If this suggestion could be accepted by the two sides, the RMB exchange issue could finally be resolved and the trade issue would also become less important in the Sino-US relation.

6. Concluding remarks

China is in a process of new transition in both domestic political and economic development. Politically, the new leadership change is approaching with great political sensitivity. Economically, China is trying to shift its economic development pattern and facing great international competition from both developed countries and new emerging economies. China will continue to pay more attention to the domestic and regional instead of global issues. But with the increasing economic power and global influence China will receive stronger pressure from international community to become a more responsible power.

China's preference to internal affairs and regional relationship has great impacts on EU-China relations. On the one hand, China will reduce its expectation to the role of the EU. On the other hand, the Western powers, especially the EU should not expect too much on China's global role. Strategic patience will be the common word for both China and the EU for dealing with the bilateral relationship.

7. Endnotes

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Chapter 5

China's Priorities and Strategy in the China–EU Relations

Zhimin Chen, Bingran Dai, Zhongqi Pan and Chun Ding

1. Introduction

Today, the relationship between the European Union and China is strong and important, though it is not in the most desirable situation for both sides. After the rapid and marked developments during the 1995–2005, recent years have, however, witnessed a number of setbacks, creating some acrimonious feelings on both sides. As the world is embracing a more challenging future after the severe world financial and economic crisis, and in view of EU's new foreign policy mechanism enshrined in the Lisbon Treaty that is taking shape, it is time for the EU and China to engage in a more serious and in-depth dialogue, so as to contribute to a possible revitalising of this important relationship.

In the following sections, the authors intend to identify EU's place in Chinese foreign policy thinking in the past, to assess the development of their relations, outline the priorities in China's EU policy, and frame a Chinese strategy towards the EU.

2. Europe in China's foreign policy thinking in the past

The EC/EU and its member states have occupied a prominent place in China's foreign policy thinking since the early 1970s. Firstly, since China and all major Western European countries established normal diplomatic relations at the beginning of the 1970s, Europe has been regarded as a group of countries without fundamental conflicting interests with China. Apart from China's diplomatic skirmishes with European countries over human rights, disputes with France over its export of 60 Mirage–2000 fight planes to Taiwan and with the UK over Hong Kong handover in the early 1990s, there had been no major concerns over European infringement of China's security and sovereignty. After the settlement of the Hong Kong issue in 1997, there is no more European military presence in East Asia, and the Taiwan issue for the most part did not feature as prominently in EU–China relations as in US–China relations. Therefore, the 2003 China's EU Policy Paper proclaims: 'There is no fundamental conflict of interest between China and the EU and neither side poses a threat to the other.'¹

Secondly, China sees a good and stable relationship with Europe serve its strategic objectives from the very beginning. After China's diplomatic normalization with all of the EC member states, China and the European Community established diplomatic relations in 1975. While these steps were taken in their mutual interests, from China's side, improving relations with Europe and supporting European integration reflected the strategic thinking of China namely the 'Three Worlds' idea, which saw the United States and Soviet Union as the 'First World', and the Western European states and other developed economies as belonging to the 'Second World', and therefore as valuable partners in China's efforts to fight against the two Cold War hegemonies². Claiming itself as one member of the 'Third World' which comprised of developing countries, China supported and would like

to see the European states to integrate themselves and to forge a common policy towards the two superpowers. Such a line of thinking continued in the post-Cold War era, when China found in the United States an unruly unilateral power posing threats to China's core interests. As European countries solidified their integration process by establishing an EU with a common currency and a Common Foreign and Security Policy (CFSP), and shared China's concerns about US hyper power, Europe was seen as a natural and ideal partner in China's drive for a multipolar world. As Zhu Liqun observed, 'The importance of the EU derived from its integration is also believed to further contribute to world multipolarization, which is a trend of future development of the international structure'³.

Although China modified the multipolar world concept with a 'harmonious world' vision and put a new stress on multilateralism from 2005, multipolarization is still seen as an inevitable trend which paves the way for the functioning of multilateralism and for a harmonious world in the long run.

Thirdly, since China's reform and opening-up policy in the late 1970s, it has come to be recognized that good and stable relations with Europe would be a necessary pre-requisite for its modernization. To China's export-oriented industries, the developed European economies not only mean a huge export market, but also a significant source of much-needed investment and accompanying technologies and management skills. Over the last three decades, the rapid growth of the Chinese economy seems to have further consolidated Chinese demands in this regard.

Furthermore, the EU as a successful model of internal and regional transformation is of itself of interest to Chinese elites. As Song Xinning argues, Europe provides a several models for the rest of world, including an integration model, a neighborhood policy model, a multilateralism model, a development assistance model and a social welfare model⁴. Chinese scholars and policy makers are enthusiastically looking for good lessons from the European experiments and achievements, such as the development of a functioning welfare state, green economy, balanced regional development and the creation of European market. In view of China's tremendous challenges unfolding in the process of rapid economic development, China needs ideas and experiences from Europe to help narrow the developmental gaps between coastal and inland regions and between the rich and poor, to achieve sustainable economic development, to construct a single domestic economy out of provincial protectionism and to rebuild its social security and welfare system. As China is increasingly involved itself in the Asian regional cooperation process, this also raises the prospect that the model of European integration might even offer an example if not template of how China might deal both with greater China and with the Asian region as a whole.

3. EU-China relations during the Post-Cold War period

With the strong push from some key member states, such as Germany and France, the European Commission issued a policy paper on China, *A Long-Term Policy for China-Europe Relations*, in 1995. In the paper's view, China 'is increasingly strong in both the military-political and the economic spheres', and the developments in China 'not only have a far-reaching impact on itself, but also have global and regional implications'. Therefore, the EU's China policy should aim to promote 'the fullest possible Chinese involvement in the international arena, whether on security, political, environmental, social or economic issues'⁵. Positive developments in the following years led the Commission to issue another China policy paper in 1998, calling for the building of a 'comprehensive partnership' with China⁶. Amid the heightened concerns over American unilateralism in the wake of American invasion of Iraq, the Commission in the 2003 China policy paper further called for an EU-China strategic partnership, stating that 'it is in the clear interest of the EU and China to work as strategic partners on the international scene.... Through a further reinforcement of their cooperation, the EU and China will be better able to shore up their joint security and other interests in Asia and elsewhere'⁷. In October 2003, apparently as a direct response to the EU's China policy paper in September, the Chinese Ministry of Foreign Affairs also issued a policy paper on the EU, *China's EU Policy Paper*. This is an unprecedented move, because the Chinese government has never published any policy paper of its kind related to a country or regional group, a fact fully demonstrating the high importance, which China attached to its relationship with the EU. The paper points out that, 'despite its difficulties and challenges ahead, the European integration process is irreversible and the EU will play an increasingly important role in both regional and international affairs'. With regard to bilateral relations, the paper states that, 'there is no fundamental conflict of interest between China and the EU and neither side poses a threat to the other', and 'China-EU relations now are better at any time in history'.

Interestingly, the paper does not prescribe the EU–China relationship as a strategic one. Only in the last part of paper regarding the military aspect, did the document seek to ‘develop and improve, step by step, a strategic security consultation mechanism’. Nevertheless, the paper expressed a strong commitment from the Chinese government’s side to strengthen and enhance China–EU relations as ‘an important component of China’s foreign policy’, and to build a ‘long–term, stable and full partnership with the EU’⁸. One year later, leaders from both sides claimed the relationship as a ‘comprehensive strategic partnership’⁹.

As both sides attached greater importance to the relationship, bilateral cooperation on a wide–range of areas deepened dramatically. In 1975 when China and the EC established a diplomatic relationship, EC–China trade was only around US\$224 million. In 2004, the EU surpassed the United States and Japan, to become China’s biggest foreign trade partner. With the opening–up of China to the global economy, in 1980, China’s trade with the EC increased to US\$6.033 billion. That figure further increased to US\$ 15.925 billion in 1990 and US\$71.514 billion in 2000¹⁰. In 2008, total EU–China trade reached US\$425.6 billion, accounting for 16.6% of China’s total trade; and also making China the EU’s second largest trade partner after the United States, and its biggest source of imports. Even when faced with the economic downturn around the world, both China’s exports to and imports from EU grew by 19% in that year¹¹.

The EU is also a major source of foreign direct investment in China. Over the last three decades, annual EU countries’ actual utilized direct investment in China rose from zero to the peak level of US\$5.44 billion in 2006, with a share of 7.48% of China’s total FDI in that year¹². EU companies have invested over US\$ 70 billion in China, and they have generated total sales of over US\$ 130 billion in 2006¹³. European investors, like their American counterparts, tend to bring in bigger, less numerous, higher value–added and high –tech projects, which had a ‘catalytic impact’ on China’s development¹⁴.

In the process, both sides have established a web of regular dialogue mechanisms, making the relationship a highly institutionalized one. Starting from 1978, with the ministerial EC–China Joint Committee is overseeing the bilateral commercial relationship, and the two sides have established more than 27 sectorial agreements and dialogues, covering subjects like climate change, regional policy, maritime transport, tourism, space science, the EU’s research and development programmes, university links, social security reform and the convergence of product standards. In 1998, the annual EU–China summit dialogue convened its first meeting. In February 2003, the Chinese foreign minister met his EU counterparts in Beijing. Thereafter, ministerial level dialogue gained an independent status, generally held in China or the country holding the EU presidency, rather than at the margins of other multilateral events. At expert level, several CFSP working groups have engaged in regular meetings with Chinese experts on issues like human rights, non–proliferation, conventional weapons exports, and Asian affairs. In September 2008, the 8th China–EU summit injected further important impetus into the development of the political dialogue mechanism by setting up the regular vice ministerial–level strategic dialogue. Since the first meeting held in London in December 2005, as of the first half of 2009, four rounds of such meetings have been held. Modelled after the US–China Strategic Economic Dialogue, the EU and China launched in April of 2008 annual EU–China a High–Level Economic and Trade Dialogue, with the participation of more than one–third of the commissioners from the EU side and a number of key Chinese ministers, co–hosted by Chinese Vice Premier Wang Qishan and EU trade commissioner Peter Mandelson. The new high–level mechanism aims to provide much needed leadership and coordination in dealing with a very complicated and challenging economic relationship.

With the EU having acquired a role in foreign and security policy, EU–China cooperation started to expand to political and global aspects. After resolving the dispute of arms sale to Taiwan by the French government in 1994, the EU and its member states in general adhered to a One–China policy, therefore sidelining the tension–producing Taiwan issue in EU–China relations. In March 1998, the EU’s General Affairs Council (GAC) decided that,– the EU would ‘neither propose, nor endorse’ any resolution criticizing China in the Human Rights Commission of the United Nations. Instead, the EU will extend its constructive approach to the human rights area, and set up a EU–China human rights dialogue mechanism. Encouraged by the new desire for an ‘overall strategic partnership’, international issues were being addressed in an annual EU–China summit, growing from 4 out of 28 paragraphs of the summit statement to 13 of 36 paragraphs in 2006. Almost all the major international issues were mentioned, indicating the mutual intention to substantiate the global strategic partnership. Also in the spirit of ‘strategic partnership’, the EU and China signed an agreement on cooperation in relation to the EU’s Galileo satellite navigation programme in 2003; and later that year, French President Jacques Chirac and German Chancellor Gerhard Schroeder both publicly supported a reexamination of the EU’s arms embargo

policy against China. The rapid rapprochement between the EU and China in 2003 and 2004 led observers to proclaim a 'honeymoon' between the EU and China was in the making¹⁵.

4. The strategic partnership in rhetoric and reality

Since late 2005, EU–China relations have encountered problems in multiple areas which have turned the relationship from a 'honeymoon' into a complicated one. First of all, the two sides are disappointed with the results of a rhetorical 'strategic partnership'. It seems no breakthroughs of crucial importance have been achieved in the past few years over the negotiation for a new partnership and cooperation agreement. Bilaterally, China's efforts to get the EU to lift its decade-long arms embargo and grant China market economy status (MES) are in vain. Europeans are also disappointed with human rights dialogues, and see no progress in their market access in China and the protection of intellectual property rights (IPR). Globally, on the issue of climate change which is regarded by the EU as the most important foreign policy issue, the two sides have engaged in some cooperation projects, and have worked together to get the United States back to the negotiation table, but in the crucial Copenhagen climate change conference, the two sides found they were in a bitterly opposed position regarding emission reduction targets, finance and the monitoring mechanism. China and EU3 (France, Germany and Britain) are members of the 6-nation contact group dealing with the Iran nuclear issue, but they found they have quite different views about proper approaches to deal with Iran.

Secondly, the EU and China unfortunately find that they are in a competitive position in areas of cooperation in the past. Economic relations were seen as a perfectly complementary, and hence mutually beneficial. Trade was more or less balanced, investments from Europe supported China's development while boosting European firms' global competitiveness. However, after the EU became the number one trading partner of China, the competitive side of the economic relationship surfaced. The EU complained about its growing trade deficits to China, and more frequently resorted to trade protection measures. At the same time, the EU also stepped up its pressures on China to open its market and strengthen the protection of IPR. The 2006 Commission China policy paper issued a long list of demands to the Chinese side, labelling China as the EU's 'single most importance challenge to EU's trade policy'¹⁶. The change of tones and approaches in the EU's trade policy towards China led one American scholar to claim that the EU was adopting an Americanized style¹⁷. China's investment and participation in the development of the EU's Galileo satellite navigation programme was seen as a symbol of the 'strategic partnership'. However, a few years later, the EU changed its mind, first limiting and in 2008 finally suspending China's involvement in the development of the system. In return, China decided to launch its own Beidou satellite navigation system, and the two sides are now locked in a head-on competition for the same frequency¹⁸.

Thirdly, the two sides found themselves in disputes over new issues in the relationship. From 2005 and onwards, China's presence in Africa suddenly emerged as a new source of disputes in EU–China relations. Politically, China is widely accused by European media and a number of governments of 'supporting' rogue regimes' in Sudan and Zimbabwe, turning a blind eye to the humanitarian crisis in Darfur and the poor human rights record in Zimbabwe, and blocking western efforts to impose sanctions on both countries in the Security Council of United Nations. The EU also criticized China for its investments in the field of energy and mineral resources, portraying China as 'neo-colonialist' exploiting African resources. In terms of development assistance, the EU has argued that China's no strings attached aid to African countries has emboldened them to resist EU efforts to promote democracy and human rights in Africa¹⁹.

Fourthly, disputes which were contained in the past have resurfaced in the bilateral relations. It seems that, in recent years, the EU has turned towards a more value-based approach in its political relations with China. The European Parliament and the media have been criticizing China's human rights record, even in the honeymoon period. This is not surprising, considering the difference in the political systems between the two sides. The new development is that, a number of governments of Member States in the European Union and to a certain extent, the European Commission on human rights, also upgraded the human rights issue in their priorities in their relations with China. Leaders of key member states granted fairly official meetings with the Dalai Lama. After the mass riots in Tibet in March 2008, the torch relay of the Beijing Olympic Games in London and in Paris were interrupted, and the issue of attending the opening ceremony of the Beijing Olympics was highly politicized, with politicians attempting to link their attendance to the issue of Tibet and Darfur. To protest the French president's announced meeting with Dalai Lama, apparently also in his position as the rotating president of the

EU, China postponed the annual EU–China summit of 2009.

The last but perhaps most profound factor having a negative impact on the EU–China relationship is the worsening of public attitudes towards each other, particularly from the European side. According to the BBC polls conducted by the international polling firm GlobeScan together with the Program on International Policy Attitudes (PIPA) at the University of Maryland, between 2004 and 2008, the European perception of China grew increasingly negative. When asked whether China is a positive or negative force, more and more citizens in European countries viewed China as a negative force, such as in France (70%, up from 33%), Italy (68%, up from 40%), Germany (69%, up from 47%), Spain (54%, up from 33%) and in Britain (42%, up from 34%). There are also corresponding drops in positive views, like in France (22%, down from 49%), in Spain (29%, down from 37%), in Italy (21%, down from 42%), in Germany (11%, down from 34%), and in Britain (39%, down from 46%). Public attitudes towards Europe have been generally very positive, however in 2008, we also can identify some downward change. In 2004, 77% of Chinese regarded the EU as a positive force, but that figure dropped to 57% in 2008. With regard to single member states, the positive rating of France among Chinese citizens suffered a substantial drop, from 72% in 2004 down to 44% in 2008, while the negative rating is up from merely 9% to 45%²⁰.

5. New opportunities for a more constructive China–EU Relationship

A number of new developments over the past months present to both EU and China a window of opportunity for revitalizing the relationship.

First of all, a post–Lisbon EU new foreign policy system is taking shape and this might assist the EU in adopting a more coherent and forward–looking China policy. On 1 December, 2009, the Lisbon treaty was finally put into effect. The much delayed revised treaty offered a brand new opportunity for the EU to be a more credible international actor. The treaty established for the first time an international legal personality for the EU, it abolished the rotating presidency in the foreign policy aspect, creating a new permanent president for the European Council and a strengthened High Representative for Foreign Affairs and Security Policy, a position merging the functions previously held by the High Representative, the foreign minister of the rotating presidency and the Commissioner for external relations in the European Commission. Although it is regretful that the member states have chosen two low–profile politicians²¹, Mr. Herman Van Rompuy of Belgium and Lady Ashton of UK, to fill the two new positions, which seemingly underused the potential offered by the treaty reforms, the early months of their work has not so disappointed. With his political skill in pushing for policy convergence, Mr. Van Rompuy has had achievements in encouraging member states to reach common positions to cope with the worst financial crisis Europe has encountered in decades. Lady Ashton also successfully obtained endorsements from the member states, the European Commission and European Parliament for her plan to create a new EU External Action Service (EAS), after months of bitter internal fighting among these players. Meanwhile, the EU is looking towards to reframing its foreign policy strategy and policies, including a review of EU’s strategic partnership with China.

Certainly, the new reforms are by no means revolutionary. By their nature, they are still intergovernmental, and the task of forming consensus among 27 countries would not be an easy task as before. However, with a greater concentration of resources and policy framing capacity in Brussels, the EU is expected to play a more coherent and consistent and effective role than in the past. Particularly, China is hoping that Lady Ashton, supported by a new External Action Service, can capitalize the improving political relationships between China and member states, to help shape a more forward–looking China policy in the future.

Secondly, at the level of member states, we have seen steady progress in bilateral relations with several member states, with which China had political problems in the past. French president Sarkozy paid a high profile state visit to China in late April 2010, and attended the opening ceremony of the Shanghai Expo. During his visit, premier Wen Jiabao was quoted as saying that, his visit ‘will offer a solid political guarantee for the growth of China–France ties’; and President Hu Jintao said China–France ties have ‘opened a new page’²². In July 2010, German Chancellor Merkel led a delegation to China, and spent her birthday in Xian, accompanied by premier Wen. The new UK conservative government has sent its foreign minister and Chancellor of the Exchequer to China after assuming power early 2010.

Thirdly, economic relations between the EU and China have become more balanced in terms of mutual dependence. The EU's yearly growth rate of exports to China rose 4.1%, in contrast to an overall decline of 16.4% in 2009. From January to April 2010, the EU's overall exports increased by 16.5%, with the recovering of world demand: however, its exports to China registered a 42.9% rise. At the same time, China's exports to Europe fell by 13.4% in 2009, and in the first four months of 2010, they only grew by 11.7%. As a result, by April 2010, China has surpassed Switzerland as the second largest market for the EU after the United States, while it continues to lead in terms of exports to the EU; more significantly, in the first four months of 2010, trade between EU and China was only 10% less than EU-US trade, which indicates that China may soon overtake the United States as the largest trading partner with the EU²³. In terms of trade balance, China's gap narrowed from 169.5 billion Euros in 2008 to 133.0 billion Euros in 2009, a reduction of more than 20 percent; and using Chinese statistics, the trade surplus with the EU fell to 108.4 billion US dollars, a fall of 32% compared with 2008²⁴.

Another much talked about issue is that of the RMB's exchange rate. Due to the financial crisis in the Euro zone, the Chinese RMB has appreciated more than 10% in 2010 against the Euro, thus removing to a large extent the issue of RMB value in bilateral relations. Rather, as China continues to support the Euro, the issue of how the two sides can cooperate in order to maintain the stability of the Euro has become a new area for bilateral cooperation. In June 2010, China's State Administration of Foreign Exchange, or SAFE, which manages the reserves under the auspices of country's central bank, was allocated up to 400m (\$505m) of Spanish 10-year bonds in a debt deal, which was seen by the market as 'a big vote of confidence for the Eurozone', and buoyed the broader markets, helping global equity rally and marking a potential turning point for the Eurozone²⁵.

In the field of foreign direct investment, China has been mainly a receiver of EU FDI for three decades, but recently, China's FDI in Europe is expanding at an astonishing pace. In late 2009, China's state shipping company Cosco took control of two container terminals at Piraeus in Greece under a 3.4 billion 35-year concession deal. In June 2010, as Moody's downgraded Greek debt to junk, Chinese companies signed a series of deals with their Greek counterparts in the areas of telecoms, and shipbuilding which were worth more than 500 million²⁶.

In early July 2010, the European Commission approved the takeover by the Chinese Zhejiang Geely Holding Group of the Swedish carmaker Volvo from Ford Motor Co. Geely, which acquired Volvo in earlier 2010, has said it is spending \$2.7 billion on the takeover, including about \$900 million in working capital to improve Volvo²⁷.

Lastly, as the world moved towards a more balanced world of multi-partnership, it is become more and more indispensable for the two sides to develop stable and closer relations, in order to nurture the benefits from the network of partners of each side. The arrival in the White House of Mr. Obama as the first African American President in American history is surely a landscape shift in American politics. Amid the setbacks of the Bush administration's foreign adventures in Iraq and Afghanistan, the tainted global image of the United States, and the most severe economic and financial crisis the United States has faced since the Second World War, President Obama arrived with a new pragmatic approach to the pursuance of American foreign policy goals.

The sense of new pragmatism also leads the Obama administration to pay higher attention to engaging the new emerging powers in an increasingly multipolar world. Certainly no Chinese observer is thinking that such developments represent an American intention to cede its leading position in the world, but rather it is seeing as a new strategic approach to retaining that position in a newly emerging multipolarising world, described as the 'multi-partner world' by Secretary of State Clinton²⁸.

President Obama abandoned the plan to deploy the anti-missile system in Poland and the Czech Republic, in order to 'reset' its relationship with Russia. In November 2009 in Beijing, President Obama and Chinese President Hu Jintao pledged that the two countries 'are committed to building a positive, cooperative and comprehensive U.S.-China relationship for the 21st Century, and will take specifications to steadily build a partnership to address common challenges'²⁹.

The retreat from unilateralism by the United States, along with the rise of the emerging powers, is transforming the world into one of multi-partnerships. Power is more balanced, and major players are seeing each other as essential partners in their efforts to develop their economies as well as jointly to deal with global challenges. If some Europeans had the illusion in recent years that working with a more collaborative American government can solve most of the pressing issues that the EU has faced, now it is increasingly realized that the EU itself also has to engage with the emerging powers with a more serious and constructive approach. There is a sense in

Europe, a feeling that the United States is one-step ahead of Europe in pragmatically adapting itself to the new changes in the international system, and Europe has to catch up³⁰.

6. Current Chinese priorities in EU–China relations

In view of the difficulties over the past few years and new recent positive developments, the Chinese side needs to articulate its policy priorities towards the EU. The following discussion presents our personal views in this regard.

1) As the EU's foreign policy system is undergoing major change, the starting point of China's aspiration in China–EU relations is to hope that the EU can play a more credible and constructive role in international affairs. For this, the Chinese side can do nothing to influence the EU; it is for the EU itself to decide. Nevertheless, the Chinese side would hope that the Lisbon reform would help the EU to have a stronger capacity in framing and implementing a common policy, not only in policy areas where supranationalism prevails, but also in foreign and security policy areas where intergovernmentalism continues to dominate decision-making. As we discussed earlier, a number of difficulties arose in the past due to the inability of the EU to come up with a common policy, or when times changed, to ensure the necessary policy adjustment. The Chinese side would hope that the EU, with the help of the new EAS, can enhance the credibility of the EU in foreign policy, be able to think strategically, and act accordingly.

Besides the internal improvement of its actorness, the Chinese side would like to see the EU act as a more constructive player in the international system. This means that China would like to see the EU acting as a system balancer whenever the remaining superpower is or intends to act recklessly; as a system maintainer to ensure the smooth functioning of the current international system and as a system reformer so that the international system can adapt to deal with the pressing new challenges in the context of the rise of emerging countries.

In terms of system maintenance, China now has a huge stake in the existing international order, the UN system, the WTO trade order, and in the financial order based on the IMF and the World Bank. The effective functioning of this system is of vital importance to China's domestic development and international engagement. Therefore, China needs the EU to play a significant role in building and supporting the current system. System balance demands that the international system should be a multi-polarized one where no single power dominating the system. To pursue that goal, China needs the EU to play its part as one of the major players in the world, using soft balancing tools, to ensure that the remaining superpower will not resort to unilateral and hegemonic foreign policy. Certainly, China does not want to see Europe and China forming an anti-US axis, because China itself does not want that, and China also believes that the Europe would not do that, and the US would not allow it to happen. Furthermore, as a new comer in the system which was not involved in the designing of most of the existing systemic institutions, China would continue to seek necessary reforms of the existing institutions, to give more voices and influences to China and other developing countries, and hence the demand for system reform. To achieve this goal, China would hope that the EU could see the change in world, and then act strategically and pragmatically, through cooperation with emerging countries, to accept the necessary though gradual system reforms, such as the creation of new institutions, like the G20, redistribution of voting powers such as in the IMF and the World bank and the rewriting of rules to suit the aspirations of the developing countries.

2) China would like to advance the bilateral relationship into a Strategic Partnership in the real sense. Most importantly, the two sides should make efforts to enhance mutual political trust. China would expect the EU to behave as a real partner, which means, at the very least, that the EU would respect China's sovereignty and the Chinese domestic system, and not interfere in China's domestic affairs, and in its handling of the Taiwan, Tibet and Xinjiang issues. The Chinese side should welcome a constructive dialogue with the EU over the domestic governance of both sides, but the EU side should end its game of naming and shaming of China on the grounds of China's so-called human rights record. Such an approach, excepting letting the Europeans feeling good internally, has done a little in the constructive sense. Moreover, China would hope that the EU can make serious efforts to strengthen the relationship, like lifting the outdated arms embargo against China, which puts China in the same group of countries as Zimbabwe. The Chinese side would like the EU to continue to abide by its commitment to the final goal of removing the arms embargo, and to take necessary steps in that direction. Meanwhile, the two sides shall start to explore the means to strengthen military ties, such as

officer exchange, joint exercises, and training, so as to improve military trust and cooperation in peace-keeping operations around the world.

3) Economically, China would like to see the EU, China's biggest trading partner, providing open and stable market access to Chinese goods and investment; China is prepared to offer assistance to ensure the financial stability in the EU. China has been seeing the rise of protectionism in Europe against Chinese imports and inward investment. Frequent anti-dumping measures have been taken in Europe, championed mostly by southern EU member states; Chinese investment in Europe has also faced numerous hurdles in a time that Chinese companies are expanding their investment globally. One of the key issues for China, not only for economic reasons, but also because the current leadership has made it a key priority, is the granting of market economy status (MES) to China.

Since the 1990's, China is by far the number one sufferer of the EU's anti-dumping measures, and the main cause is that the EU has not given China the so-called MES. Because of this, when determining whether dumping exists, the exporting prices of Chinese exports are not compared with their domestic prices, but instead with the prices of the similar goods of another country with an established MES.

According to the GATT rules, the sole criterion of the MES is whether the domestic prices of the country are determined by the market. With more than 95% of domestic prices determined by the market, China very much qualifies for MES, but the leading developed economies including the EU still refuse to give China this status. The question is why the EU refused a re-consideration of China's application in 2004, but gave Russia this status. China is not in the least against the EU giving Russia such status, but in so doing there is apparently a double standard, and even discrimination. 2016 is not very far away when China will automatically enjoy this status, but an earlier granting of the MES to China will demonstrate the sincerity from the EU side in its efforts to develop a strategic partnership with China.

It is true that during the past decade of rapid growth, disputes and conflicts have increased as well. The top issue in bilateral economic relations seems to be the trade imbalance, that is, the rising trade (in goods and services) surplus of China against the EU, which reached its peak in 2008 of 164.7 billion Euros as opposed to the total trade volume of 361.2 billion³¹. It is indeed an imbalance, which needs to be addressed. Protection measures to limit imports from China are certainly not the right way, as they will be at the expenses of European consumers and industries alike. A better approach is for China to import more from Europe. Here the key issue is that the EU should export what China needs to import. The comparative advantage of Europe is in high-tech products; if the EU could be more open in this respect, such as relaxing its export control of so-called dual-use high-tech products, it could serve to address the trade imbalance issue.

The Chinese side has made a number of important moves to support the Euro, and has helped the Euro to rebound from its low level against the US dollar. Many of the current international financial disturbances are rooted in the contradiction between the dollar's international usage and its sovereign issue. Cooperation between China and the EU, between the People's Bank of China (PBC) and the European Central Bank (ECB) and between the RMB and the Euro may still be a political issue at the moment, but its successful development will certainly be a stabilizing factor of great economic implications. The Chinese side, having invested in Eurobonds to the tune of about 400 billion Euros, continues to see the EU as one of major destinations for its foreign currency reserve, and is willing to support the Euro as an international currency. Having said that, the Chinese side has its concern over the safety of its investment, and would like to work with the EU's institutions and member states to develop ways to ensure the safety of these investments as well as ways for China to support the Euro.

In addition, there are other important areas where China believes its relations with the EU could be further developed:

—energy and climate change cooperation: China is bound to be the world's number one energy consumer sooner or later, and that has caused great concerns both at home and abroad, especially as it is linked to the issue of climate change and environmental protection. Europe is much more advanced in energy saving, green energies, etc. Increased technological cooperation and assistance in this area will be beneficial for both and for the world at large, and with very significant economic implications as well.

—Tourist and cultural cooperation: Both China and Europe are rich in natural, historical and cultural attractions, and this is an area where consumption potentials are always rising. To realize such potentials, both sides need to

make the markets more open and to provide better information and better services. From the Chinese side, we would like to see the EU develop a speedy and simple visa application procedure, to facilitate Chinese citizens coming to visit Europe.

Education cooperation: This also has an economic aspect, and education cooperation is an investment in the future. Europe enjoys here a big advantage in attracting Chinese students, if only the language barrier could be lowered.

Government procurement: If China and EU could negotiate and reach an agreement in this area, the gradual opening of the markets will yield tremendous economic benefits for both by bringing forth their comparative advantages.

Cooperation between small- and medium- sized firms: As both sides have large numbers of such firms, the creation at the government level of a joint mechanism, including a service agency and a fund, to facilitate and support such cooperation would open a new horizon in China-EU economic cooperation.

4) Globally speaking, China would expect the EU when cooperating with China to maintain the existing international system, such as the liberal trade regime and financial lending institutions; meanwhile, China also hopes that the EU can offer support for the growing role of emerging countries, and hence the timely reform of the existing global institutions; and equally work equally in finding solutions to the pressing challenges of today's world.

One of their common challenges is the accelerated process of economic globalization. Whether we like it or not, economic globalization is a natural process and a destiny that is inevitable due to science and technology advancement and economic-social development. In macroeconomic terms, the marked acceleration of factor movements brought about by globalization entails competition at an international level, worldwide reallocation of resources, shortened business cycles –just to mention some of them– which every economy has to reckon with seriously. Issues of international scope and implications have to be dealt with together by the major players, including China and the EU. Globalization has also created new opportunities, which are likewise better exploited through common efforts.

The lesson that we all should draw from the current financial crisis is that given the changes and developments in the past few decades, the existing international institutions are no longer capable of dealing with new situations and issues, such as financial stability and security, food and energy supply, climate change, etc. Reform of the old order has proven and shall prove to be as difficult as the setting-up of a new order, and as stakeholders China and EU have a strong case for cooperation. Specifically, the EU and China should work together to consolidate the G20's status as the main platform for global economic and financial management; and they should endeavor to reform the IMF and World Bank's voting and management structure so that emerging countries can have their due influence in these institutions.

Regarding global challenges, China and the EU share common interests and goals, such as the fight against climate change, the prevention of nuclear proliferation and the promotion of stability and development in Africa and other developing world. At the same time, due to a different foreign policy tradition, different levels of development and a different experience in dealing with developing countries, the two sides must overcome a number of important differences in their efforts to achieve these common goals. Under such circumstances, the Chinese side would expect the EU to work with China to achieve progressive convergence based on equal dialogue. In this spirit, China would expect that the EU could respect China's positions on various global and regional issues, and seek cooperation with China in finding solutions to these issues, without attempting to impose European views and solutions onto China, and expecting China to accept them. The Copenhagen climate change conference was surely a bitter experience in this regard. To avoid this, the two sides need to engage in a more sensible and constructive dialogue.

7. Framing China's New Strategy for revitalizing China–EU Relations

7.1. A pragmatic yet proactive approach

China should approach the EU from a very pragmatic standpoint, based on the recognition of two realities in the international system. The first is the current complicated nature of China–EU relations. Due to the relative decline of the United States and America's return to multilateralism, neither China nor Europe would have strong motivation in upgrading their relationship for the purpose of balancing American unilateralism as they did in the past, while at the same time China and EU would find their interests would not always be in harmony as both of them aim to have a greater influence around the world. The second reality is the emergence of today's world of multi-partnership, in which both parties strive to improve their relations with third parties, thus rendering the relationship less special than it was in 2003 and 2004.

Recognizing these facts means that China should not develop excessive expectations for bilateral relations. It should emphasize the stability of the relationship, the expansion of pragmatic cooperation, and the search for ways to contain disputes.

However, a more pragmatic China would proactively make use of the window of opportunity provided by the Lisbon reforms. On the one hand, China would continue to commit itself to the 'strategic partnership' as the basic characterization of the relationship. On the other hand, it would give new life to the notion that the EU after Lisbon reform would 'become a more effective partner of China'³². Therefore, China has decided to upgrade the EU–China strategic dialogue to the same level as that of the China–US strategic dialogue, involving State Councilor Dai Bingguo and his counterpart, Lady Ashton. Although it is not at the moment known whether or not such a raising of the level of dialogue would produce more substantive results, China has at least given an important indication that China would take seriously the new foreign policy system after the Lisbon reform, and would try its best to work with the new EU leaders in foreign policy, to see if the two sides can make the most of the opportunity to move the relationship to a new level.

7.2. Multilevel engagement

The Lisbon reforms, while having strengthened the EU's international actorness, did not change the basic nature of the EU's multilevel foreign policy's system. Although the EU institutions, including the European parliament, all take on greater roles in the shaping and execution of EU foreign policy, national governments continue to enjoy significant influence in the making of EU's foreign economic policy, and maintain their power of veto in the Common Foreign and Security Policy. Furthermore, at societal level, the public, NGOs, business communities and the media also intervene as important players in the shaping of European policy towards China.

Starting from such a view of the European foreign policy system, it is important that China's strategy towards the EU be a multilevel one. Aside from efforts to engage the EU level institutions, China has to strengthen its efforts to develop stronger relationships with the member states. At the moment, a number of EU states are facing economic problems at home, and expanding their exports to a fast growing Chinese domestic market, attracting investments from Chinese companies, and seeking Chinese financial help, are of growing importance to these countries. By focusing on this positive and mutually beneficial cooperation between EU states and China, the possibility of closer economic relations is much likely and more beneficial than in previous years. China has maintained a positive relationship with the new UK government and its relations with France and Germany have also improved. Through Chinese companies making large investments in the crisis-stricken Greece economy, and in the purchase of Spanish government bonds, China is helping the countries in economic troubles. Such an overall improvement of China's relations with individual member states is important in itself. Meanwhile, it would surely give further impetus to the progressive development of China–EU relations.

One thing that is clear for the Chinese policy-makers is that the problems in China's relations with the EU over recent years have been at the societal level. With a large part of the European population holding unfavorable views about China and China's international influence, it is important that the Chinese side should make efforts to better present itself to the European public. On 1 July, 2010, China's Xinhua News Agency launched its English language TV service, CNC World. CNC World broadcasts English news programs 24 hours a day and

covers breaking news and major political, economic and cultural news around the globe. Early 2010, China's former ambassador to the United Kingdom, Madam Fu Ying, was promoted to her new position as the vice foreign minister in charge of European affairs, apparently due to her impressive public diplomacy performance. Currently, China has established more than 26 Confucius Institutes, offering Chinese language and cultural courses in EU countries. From May to October 2010, the half –year– long Shanghai Expo offered a rare but massive opportunity for the general public of the two sides to engage in extensive cultural exchanges. It is welcoming to see that positive views towards China have been improving after reaching a low point in 2008³³. However, much more work must be done in the future.

Table 1: Opinion of China

Opinion of China						
Do you have a favorable or unfavorable view of China?						
<u>Country</u>	Favourable (%)			Unfavourable (%)		
	2005	2008	2011	2005	2008	2011
Britain	65	47	59	16	36	26
France	58	28	51	42	72	49
Germany	46	26	34	37	68	59
Japan	–	14	34		84	61
Poland	37	33	51	34	54	32
Russia	60	60	63	29	26	25
South Korea	–	48	–		49	–
Spain	57	31	55	21	56	39
United States	43	39	51	35	42	36

Source: Pew Research Centre ‘Pew Global Attitudes Project’ 13 July 2011

In June 2010, the Germany-based Heinrich Boll Foundation sponsored research on how China was reflected by the main German media in 2008. The study's authors argue that German reporters often miss the chance to present new perspectives to their audience, and the perception of China as a competitor has become so widespread in the West that many journalists also follow this pattern³⁴. As the German case indicates, negative reporting of China has played a role in producing an excessively unfavourable view of China in the European continent, while people in the UK and the United States generally hold a more balanced view of China. It is for this reason that Germany and China are paying more attention to the improvement of dialogues between media from both sides.

It is also noted that the lack of expertise in Europe on contemporary China studies is becoming an issue in the development of healthy China–EU relations in this more complicated stage of the bilateral relationship. Years ago, David Shambaugh, an American scholar, lamented the small number of China specialists in Europe, particularly in comparison with the United States³⁵. The result of that is that either policy makers are not supported by sophisticated policy advice, or there are not enough voices from the expert community in the media to provide balanced views about development in China. Surely, a remedy to that must be a long-term task and it should be mainly a job for the European governments and societies to improve their China studies capacity. For the Chinese side, while appealing for the EU to commit more investment in training a new generation of researchers, it can contribute by expanding research exchange and help train future scholars by offering an advanced degree programs both in Chinese and English in the Chinese Universities, or by developing joint degree programs with European universities.

7.3. Global Perspective

China–EU relations are not isolated bilateral relations. Sino–European relations in the past were subject to the constraining effects of the superpowers, and in the future they will be affected by changes in the international

structure and their respective relations with other major players. At the same time, as both China and the EU acquire greater influence in international affairs, and their bilateral relations are increasingly globalized, both sides will need a global strategy to conduct their relations with each other.

In relation to China's global policy towards the EU, on the one hand, China should continue to put the EU in the central position in its global strategy. With a Union of 27 member states, an economy of the same size as the United States, EU is the biggest trader and investor in the world, and wields significant influence in world affairs. Developing cooperation with the EU, not only is important for China's continued development, but is also the key to finding solutions to various regional and global problems. China, together with the EU, affirmed that, "The EU and China, as comprehensive and strategic partners sharing much common ground on international issues, seek to actively meet global challenges and strive for a peaceful, sustainable and prosperous world which cannot be achieved without the joint efforts and close cooperation of the EU and China"³⁶.

On the other hand, as China's own international influence continues to rise, being an indispensable force in the world's major institutions, like the Security Council of the United Nations, the G20 summit, the World Bank and IMF, with prudent but proactive diplomacy, China has shown that it can maintain cooperative relations with other major powers and with the majority of the developing countries. Even with the remaining superpower, the United States, China has managed to have a workable relationship with both the Bush Jr. administration, and the current Obama administration. Although faced with a number of key issues dividing them, the two countries have developed a series of highly institutionalized channels to address their disputes as well as to work for their common interests, which has given rise to the notion of the 'G2'. Officially, Chinese leaders have stated on a number of occasions that China rejects the idea of the 'G2'. In the meeting with President Obama in November 2009 in Beijing, Mr. Wen outlined three reasons why China rejects the idea. First, China is still a developing country; second, China pursues the independent foreign policy of peace and will not align with any country or country blocks; third, global issues should be decided by all the nations in the world, rather than one or two countries³⁷. Having said that, the Chinese government certainly understands that an improved relationship with the United States is not only important in itself, but will also reduce the room for Europe to ally with the United States in jointly forcing China to accept deals that it dislikes, a popular idea among a certain circle in the west, as indicated by the misleading policy paper from the European Council on Foreign Relations (ECFR)³⁸.

Similarly, China will continue to strengthen its relations with countries around the world. With its partnership strategy in place from 1993, China has established more than thirty strategic partnerships with key states in the world, including a number of EU member states. Over the last 10 years, it also developed partnerships with regional blocs, such as the China-ASEAN Partnership, the China-EU Partnership, the China-Africa Partnership through the Forum on China-Africa Cooperation (FOCAC), and the China-Arab Partnership through the Sino-Arab Cooperation Forum (SACF) established in 2004 between China and the League of Arab States, a regional organization with the membership of 22 Arabian states. China also initiated or participated in a number of multilateral platforms based on China's bilateral partnerships, such as the China-Russia-India trilateral mechanism, the BASIC Network involving China, Brazil, India and South Africa, which played a vital role in the Copenhagen Climate Change Conference, BRICS (including Brazil, Russia, India, China and South Africa) Summit, the China-Japan-Korea Trilateral Partnership and Mechanism, and the Shanghai Cooperation Organization (SCO). Through this web of bilateral and multilateral partnerships, China is able to forge stronger ties with a majority of the countries around the world. With China's expanding presence and growing influence in the world, this will create more incentives both for China and the EU to enhance dialogues and cooperation between them, rather than indulge in a mutually disadvantageous game of competition.

8. Conclusion

To conclude, we think there is still room for the China-EU relations to be further developed, and we have a window of opportunity before us. It is certainly true that, as the relationship enters a more complicated stage, it will be difficult to make dramatic changes. However, if we can grasp the new opportunities, think strategically, and act pragmatically, the relationship could be enhanced in the near future.

In strengthening this important relationship, China needs to take a pragmatic yet proactive approach. In the context of the complicated nature of China-EU relations, China should not expect any easy breakthrough in

their relationship. At the same time, China shall act proactively, grasp the opportunities offered by a new EU foreign policy system, growing desire of some EU member states to improve cooperation with China amid European debt crisis, and also a warming-up public opinion.

In addition, China should engage the European side from a multilevel approach. Apart from working with various EU institutions, China should also make further efforts in consolidating its relations with member states, better present itself to the European public and attempt to enhance Chinese expertise in Europe.

As Europe is developing a global China policy, China shall also develop its global EU policy. Closer and stronger partnerships with main players in today's world would add incentives for the EU to work with China. In this regard, there is much to do for China in the context of growing disputes between China and some of its neighbors, and between China and the United States in the past two years.

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Chapter 6

China's Foreign Policy: A European perspective

Fernando Delage and Gracia Abad

1. Introduction

China's rise is arguably the most relevant development in contemporary international relations. The steady economic growth of the People's Republic of China (PRC) over the past three decades, its deepening integration in the global system, as well as its high level of defense spending have enormously increased Beijing's influence. In the space of two generations, China has become the world's second largest economy and besides playing a major role in Asia, China's diplomacy is also active in the Middle East, Africa and Latin America. Hardly any issue in the global agenda, from climate change to financial reform, from nuclear proliferation to energy security, can be addressed without Beijing's participation.

Both in the PRC and in the world at large, China's re-emergence has stimulated a debate on its implications for the international system, and for the country's foreign policy. It is only natural that analysts ask themselves what role China is playing in reshaping the world order, and what its place is in that order¹. In a nutshell, they question whether a more powerful China will be a peaceful and responsible member of the international community, or will it throw its weight around and challenge current rules. Those of a liberal persuasion predict that the forces of economic interdependence will turn China into a constructive international partner, while many realists, in contrast, believe that the PRC's economic growth will inevitably lead to a similar development of its military power and will, in due time, challenge the existing order.

Since the ascent of China is taking place in an international order characterized by unipolarity due to the preeminent position of the U.S.², the discussion usually focuses on the PRC as a potential challenger to American hegemony. The United States is indeed the main variable affecting China's view of the world, and the critical factor in the shaping of its national security strategy. Likewise, China's rise is the main foreign policy concern of the United States in the longer term. It is against this general background that the Sino-European relationship must be considered.

Despite its economic and political weight, Europe is not an element of the Asian balance of power, and has no direct strategic interests involved. However, the changing distribution of power in the region, of which China is the main driver, will affect global equilibrium and therefore Europe enormously. The impact of China's economic growth and energy consumption has been affecting international markets and politics since the 1990s. In 2004 the European Union became the largest trading partner of China, a country with which it has a giant trade deficit, and promises to be an important competitor to its high tech manufacturing. Many Chinese companies are already investing in Europe, and are likely to do so on a larger scale in the future. The rise of China also affects Europe because of its impact in the setting of rules for global governance as well as on human rights issues. At the same time, China's role is growing in many parts of the world, like Africa or the Middle East, where previously its interests were limited, while Europe played an important role. In a word, 'China is now a factor in every global issue that matters to Europeans'³ and as China's presence and interests throughout the world expand, so will the policy challenges for the EU.

The global financial crisis has probably accelerated the ongoing power shift towards China and other emerging large economies⁴. If the PRC is the big winner of the crisis, the EU is among its greatest casualties. Europe's international influence is diminishing, while that of China is growing. Add to this the bilateral strains over the past few years and the lack of a coherent and coordinated European position on major foreign policy issues, and the result is a sceptical attitude in Beijing towards the EU as a global political actor. If for a time Europe seemed a good partner for China to try to balance the United States or, at least, try to promote a multipolar world order, strategists in Beijing see no room today for the EU among the great powers⁵. Instead, they increasingly see a formerly robust economic power struggling to remain afloat.

As Europe reassesses how to respond to China's rise, nothing is of course more important than shaping an integrated EU approach rather than maintaining different national policies vis-à-vis the PRC. But even a coordinated strategy requires three things to succeed: a clear understanding of the role the EU plays in Beijing's diplomacy; a thorough grasp of their respective perceptions of the international system and the roles they play in it; and a systematic examination of the implications of China's re-emergence for Europe's global interests. These three issues are considered in this chapter, after first taking a quick look at the historical background of the Sino-European relationship to better appreciate its current travails.

2. China and the European Union: a brief history

Although China and the then European Community established relations in 1975, the PRC's concern with its security in the context of bipolarity assigned Europe a mere 'secondary role' in its foreign policy during the cold war⁶. It was only in the following decade, with the launching of economic reforms in China, that Beijing started to cultivate relations with a number of European states. In 1985 a legal basis was provided for the Europe-China relationship through the Trade and Cooperation Agreement, a document still in force.

From the mid-1990s, a changing global political and economic landscape drove Europe and China to adjust their relationship. With the end of the cold war and the adoption of the 1993 Maastricht treaty—which added the construction of monetary union and the shaping of a common foreign policy to the just completed single market—China realized that the EU was becoming a major international force. For its part, the European Union also began to show a stronger interest in China as a market and as a political partner. Against the background of a new Asia strategy which it had developed a year earlier⁷, the EU issued its first strategy paper on China in 1995⁸. The first EU-China annual summit meeting took place in 1998; since then, Sino-European relations have developed rapidly although many ambiguities remain in their mutual perceptions.

If the EU and China came to recognise each other as an emerging force in international affairs after the end of the cold war, with China's entry into the WTO at the end of 2001 and the introduction of the Euro in January 2002, both parties developed a greater interest in deepening their partnership. Bilateral trade grew rapidly, and both China and the EU issued major policy documents in 2003 that aimed at a strong bilateral relationship. In October China published its white paper on EU policy, an unprecedented document⁹. It was the first time that the Chinese government published a text that defined the country's policy towards a specific region of the world and listed the objectives that both sides should achieve in order to strengthen the relationship. China showed a great interest though it remained 'conscious of the absence of a strong and comprehensive mutual understanding'¹⁰. Only a month earlier, the EU had defined China as a strategic partner in a new policy paper¹¹. At the annual summit held the same year, the first attended by Hu Jintao as new president of the PRC, both parties agreed on launching their 'comprehensive strategic partnership'.

It was obvious to both China and the EU that besides addressing bilateral questions, they should also 'discuss regional and international issues of common concern'¹². However, in 2004 and 2005 things started to go wrong. Most importantly for Beijing, it failed in its request to have the EU arms embargo imposed on China for the Tiananmen crackdown in 1989 lifted: American and Japanese pressures made Brussels change its mind on the ending of the prohibition in the summer of 2005. Although the EU remains committed to removing it, no advance has been made to this date. As defined by the Chinese, the embargo is an act of discrimination which complicates the full realisation of their strategic partnership¹³.

Despite these difficulties, the European Commission adopted in October 2006 a new policy paper, which outlined the EU strategy for responding to the PRC's growing strength¹⁴. Very soon however, the relationship

further deteriorated. Trade and economic ties grew tenuous as Europeans began to feel the impact of economic competition with China. The EU's trade deficit with China reached 150 billion in 2007, a jump of over 25 percent from the previous year. In July 2007, speaking at the European Parliament, the European trade commissioner, Peter Mandelson, declared the bilateral relationship to be at 'a crossroads', and emphasized that China should act to meet its WTO commitments, remove barriers to EU exports, protect intellectual property, and stop dumping practices. In August, the EU also took the decision to diminish its development aid to China.

The breadth of the Joint Statement of the 10th EU–China summit (November 2007), a document outlining bilateral views and activities ranging from political dialogue and the role of the United Nations, to counterterrorism, economics, regional issues such as Iran, North Korea, Darfur and Burma, as well as educational and cultural exchanges, reflected the wide range of problems the EU and China intended to address jointly. But during the summit, Mandelson again publicly denounced Beijing on a number of market access problems, and there were strained discussions on the value of the Renminbi (RMB), the arms embargo, Africa, and Chinese human rights practices.

Around this time, new leaders in Germany, France and the UK decided to take a tougher attitude towards China. Shortly after a trip to China in August 2007, Chancellor Angela Merkel met with the exiled Tibetan leader, the Dalai Lama, in Berlin, resulting in a strong response from Beijing and the suspension of high-level Sino–German contacts. In 2008 European governments were tainted with the problems of the Olympic torch procession through London and other capitals. In Paris a disabled Chinese athlete was attacked by protestors who accused Beijing of encouraging the Tibetan riots of March 2008. At the end of the year, China cancelled the regular summit meeting with the EU after French President Nicolas Sarkozy met with the Dalai Lama. One year later, in December 2009, China executed a British citizen for drug-smuggling—the first European to be executed in China in 50 years—despite condemnations from European governments and pleas that he be spared because of his mental illness. The same month, at the Copenhagen UN climate change conference, EU leaders were shocked by China's disdain for European efforts at securing a binding commitment to cut emissions.

The Copenhagen conference is in fact viewed by some observers as the final straw for those European policy-makers who advocated engagement with China. After Copenhagen, European attitudes have hardened and governments are reconsidering their approach to the PRC¹⁵. Simultaneously, the clashes of the last few years have also changed the Chinese perception of Europe: Beijing has focused more on managing its bilateral relations with individual countries than with the EU at large, and seems to have renounced to the possibility of using the EU to counterbalance the United States.

Europe and China find themselves at a complex crossroads in their relationship. In a globalizing world, the two sides have an increasing contact in a growing number of places around the world, and with a growing list of economic and political issues. EU–China relations have become more difficult to manage and also more tense as a result of the European trade deficit, China's exchange rate policy and market access problems, and differences on global governance and human rights. In brief, in a context of emerging difficulties, both sides are developing a new perception of each other, and their relationship is moving from the 'honeymoon' of earlier this decade to a more realistic stance¹⁶.

3. Europe in China's foreign policy

The Chinese generally have a positive view of Europe. They have the highest regard for its cultural richness, higher education and business practices as well as for the integration process itself. The single market, the Euro, and EU's enlargement are viewed with particular admiration. Beijing's assessments of relations with Europe are equally favourable: as the 2003 China's EU policy paper puts it, '[t]here is no fundamental conflict of interest between China and the EU and neither poses a threat to the other¹⁷'. Unlike the United States, Europe is not a strategic rival; however, China thinks of the EU primarily in economic terms.

Ever since China's reform and opening up in the late 1970s, Europe has been one of its most important trade and economic partners. China needed the investment, technology and experience of European countries. Thirty years later, the EU has become China's primary trading partner, accounting for nearly a quarter of the PRC's overall external trade in 2010. In return, China is the EU's second largest trading partner, after the United States. EU countries also provide China with a larger amount of foreign direct investment than does the United

States, and remain an important source of technology transfers (Germany is China's largest supplier of machine tools, for example). The EU and its member states have in addition provided a significant amount of technical assistance and financial aid, originally focused on improving China's infrastructures and rural development and, most recently, on environmental protection and good governance.

In trade and other economic issues therefore the EU matters increasingly for China. And it is also in this context that Chinese analysts see—correctly—the basis of Europe's international influence. Besides the sheer size of the European economy as a bloc, Chinese commentators regard the Euro as 'probably the EU's greatest institutional success', and the 'most important component of Europe's external power'¹⁸. Beyond this admiration, however, they see serious limits to economic cooperation with the EU.

China has sought unsuccessfully for the EU to recognise its full 'market economy status', a definition that would give its goods easier access into European markets by making anti-dumping and countervailing duty cases more difficult to pursue. For China, this issue remains one of the main points of contention in the relationship, along with the arms embargo. The Chinese government has pointed out the EU's contradictory stance in conferring Russia market status in 2001 but failing to grant it to the PRC. Simultaneously, Beijing faces a long list of complaints from the EU regarding market access into the Chinese service sectors, as well as the political tension provoked by the huge European bilateral deficit. In these circumstances, despite the talk about their strategic partnership and the growing number of sectoral meetings and working groups, the negotiations launched in 2006 on a new Partnership and Cooperation Agreement that would succeed the 1985 Trade and Economic Cooperation Agreement have not yet concluded.

Chinese perception of Europe's place in international politics has also evolved significantly. EU countries have a special appeal for Beijing because they do not show the same degree of distrust of China's intentions as does the United States. Whereas Chinese analysts believe that the United States wants to contain China's rise, they view European policymakers as seeking to engage China and promote its stable development¹⁹. Instead of focusing on China's military modernization, European instead intends to see a large country going through a complex social and economic transformation. They may have different understandings of human rights, but this has not become a barrier to the development of bilateral relations. Additionally, Europe does not have military forces stationed in East Asia and does not have the geopolitical ambitions of the United States. When it comes to Taiwan, the Korean peninsula or the US–Japanese alliance, Europe is no more than a spectator. It is no wonder therefore that from China's perspective there is no strategic conflict of interests between the two sides. Accordingly, developing closer relations with the EU has been viewed by Beijing as providing more options and more room for manoeuvre²⁰.

China attached considerable significance in particular to the role of the EU in shaping a more multipolar world, and saw the transatlantic rift over the Iraq war as a unique opportunity to expand its engagement with the Europeans. Beijing considered the EU to be an independent political actor and economic powerhouse whose interests did not necessarily always coincide with those of the United States. With the deterioration of United States–Europe relations in the early 2000s during the Bush administration, analysts saw the EU–China relationship as part of a new restructuring in global power relations. A new Sino–European axis or a 'strategic triangle' between the United States, the EU and China could be created, both of which would weaken American influence²¹.

Despite China's expectations, its unsuccessful effort to persuade the EU to lift the arms embargo in 2005 taught Beijing some lessons on the limits of the bilateral relationship. Regardless of their important economic ties, China realised that, politically, the EU lacks a single, unified voice in the international arena. Its limited autonomy vis-à-vis the United States on strategic issues further reduced its attractiveness to Beijing as a potential diplomatic partner. In the words of a Chinese expert, however much Beijing would like to see a stronger Europe becoming one of the poles of an eventual multipolar order, 'the American factor provides a long-term external constraint on any EU–China strategic partnership'²².

As Jean–Pierre Cabestan writes reviewing the Chinese literature, some analysts hold the view that the EU 'is essentially an economic union', and cannot be considered as a pole since it has not yet developed a credible integrated military force and it is constituted of nation–states that have jealously kept much say on foreign and security policies. Others remain very realistic about the benefits for China: 'The EU will not change its alliance with the United States and the NATO framework will continue to dominate their relationship. It is

basically because both are market economy democracies with homogeneous values. This makes the EU a more independent competitor but not a challenging adversary of the United States²³. In fact, the United States and the EU not only share fundamental values, they also pursue similar objectives with regard to China: integrating it into international institutions and engaging it to become more involved in terms of non-proliferation, climate change, international security and human rights. This means that from a strategic viewpoint, there is no triangle between the EU, the United States, and China, and not much chance of seeing one take shape.

Given the EU's experience in a variety of policy areas that are relevant to Chinese domestic development, the PRC has largely seen Europe as a useful friend and a valuable adviser. However, it did not see the EU as a real player internationally, except in economics. A situation which is even worsening for an EU severely hit by the global economic crisis. For the Chinese there is a sense that the EU is much less politically than the sum of its parts, that it lacks a strategic vision and suffers from internal division, which limits its global weight. Europe simply does not exist as a political centre of power, especially compared with the United States²⁴. With the exception of trade and finance, Europe's international influence is to a great extent based on its role as a 'normative power', something which precisely clashes with China's sacrosanct adherence to the principle of absolute sovereignty (see below).

In these circumstances, Beijing has made consistent efforts to expand its relations with major EU member states. It has reached bilateral 'strategic partnerships' with France, Germany, Italy, Portugal, Spain and the United Kingdom. Since 2005, China's bilateral diplomacy has become a prominent feature of its Europe strategy. Beijing realised it could gain more leverage by working bilaterally, including by playing European countries off one another²⁵. For the Chinese there are severe limitations to seeing Europe as a united and coherent force in the world. As a Chinese observer put it: 'There are still 27 individual China policies behind the strategic partnership that the EU is seeking with us. What matters more is building up our bilateral relations with the major European nations, each of which has different ways of dealing with the Chinese government'²⁶.

What seems to emerge is in summary a fragmented Chinese perception of Europe. Strategists in Beijing feel a united Europe would fit into their concept of a multipolar order, however, in order to play that role, the EU should develop a much more coherent foreign policy. Although that is precisely one of the main purposes of the institutional reforms put forward by the Lisbon treaty, many Chinese observers remain sceptical as to the EU's ability to overcome its internal differences and lack of strategic leadership. However, as we pointed out above, the global economic crisis and its impact on Europe are making things even more difficult for Europe. The PRC has found a window of opportunity as many EU countries are interested in attract foreign direct investment (FDI) and find buyers for their bonds. Nonetheless that will make for the EU much harder to develop a truly common and coherent policy towards China as many of the member countries are rallying for—even competing among them— Chinese investments, Chinese will to buy bonds from different countries as well as for Chinese availability to take part in 'public procurement'²⁷.

4. China, the EU, and the international system

In the late 1970s, Deng Xiaoping and other Chinese leaders were convinced that only by joining the international order could China overcome its backwardness and develop its economy. Given its size, the PRC had an enormous potential, but it lacked a solid internal base to acquire the economic and military weight necessary to be considered as a great power. Accordingly, together with the reform and opening policy, the building up of 'comprehensive national power' (*zonghe guoli*) would become one of the fundamental goals of China's strategy²⁸.

In its search for great power status, China has not only deepened its integration in the international order—it has joined around a hundred international organizations and signed over 300 treaties'²⁹ but it has also turned itself into a crucial actor in the reshaping of that order. This fact cannot be underestimated when shifts in the balance of power are taking place, and the competing world visions and interests of the different actors, as well as their ability and capacity to uphold them, will determine the rules and nature of the future international system.

What are the features of the world order preferred by China? To what extent do they coincide with those upheld by Europe? The answer to these questions depends on whether China is satisfied with the current international order or would prefer to challenge it. In other words, is China a revisionist, 'adversarial power', or does it defend the status quo?³⁰ In very broad terms, China seems to be trying to develop a multipolar international order capable of restraining the United States without seeking to challenge the United States itself; an approach that would not seem to be very much in contradiction with that of the EU.

This potential convergence is regularly referred to in the Chinese official discourse on Europe. Speaking in Hamburg in the Autumn of 2006, for example, the prime minister Wen Jiabao said:

'China–Europe relations have a solid base. Both sides share many common views in politics. China and Europe pursue multilateralism and stand for democratizing international relations and protecting the authority of the United Nations. Based on their common interests and reciprocal needs, China and Europe have strengthened and will continue to strengthen their cooperation so as to achieve the goal of trusting each other politically, making their economies complementary to each other, conducting mutual cultural exchanges, and engaging in common development'³¹.

Only a year later, foreign minister Yang Jiechi would insist again that the two sides do not have a fundamental conflict of interest or 'outstanding historical issues' standing between them, and that they both 'advocate multilateralism and support upholding the authority of the United Nations'³². Indeed, European and Chinese views defend a greater role for the United Nations and other multilateral organizations, and generally seek a more 'multipolar' world. In this regard, the EU has consistently favoured an increasing Chinese participation in UN peacekeeping activities. By January 2008, the PRC was the largest contributor to UN peace operations among the five permanent members of the Security Council.

Likewise, China may well be in favour of a rules based international order which reduces uncertainties, enhances predictability and helps it to protect its growing global interests.³³

Although the PRC and Europe may have similar interests or views on a wide range of issues regarding the international system, their differences cannot be overlooked. This is the case, for instance, of the concept of sovereignty. Although China was a latecomer to Westphalian nation–state diplomacy, Chinese leaders have anchored their security and diplomatic practice in a rigid concept of sovereignty. At a time when European leaders stress the interdependencies that have eroded political and economic sovereignty, Chinese leaders stubbornly cling to absolute principles. Beijing argues that concern for human rights, even genocide, can never override inviolable principles of sovereignty, and that sovereignty is the last defence of developing countries. China thus condemns the doctrine of intervention, while its leaders do not seem to support the doctrine of the responsibility to protect. On its part, the Europeans insist that sovereignty can never preclude the respect of human rights or prevent human rights issues from being effectively addressed. The war in the former Yugoslavia in the late 1990s clearly proved this divergence: by emphasizing Serbian sovereignty over its treatment of the Kosovars, China appeared to be the conservative power, defending a traditional order of state rights, while Europeans seemed to be trying to reshape the international order, making the concept of sovereignty conditional on good governance.

This is a good example of perhaps the main difference which shapes the whole EU–China relationship: China is a pragmatic and realist power while the EU is first and foremost a normative power, a defender of liberal institutionalism. This fact determines the ways in which the two sides approach each other. The Europeans, already struggling to reconcile their normative agenda—the promotion of an ethical approach to international relations and defence of human rights—with their material interests as a whole, face at the same time the challenge of a rising China, an emerging power with a strategy aimed at the pursuance of its national interests, often hidden within the goal of 'de–Westernizing' global politics³⁴. More often than not, the Chinese strategy clashes with European priorities. Their respective views on multilateralism and human rights are two cases in point.

Many European nations share China's defence of a more multipolar international order but interpretations of this goal differ. Multilateralism is indeed a clear example of something that both the EU and China pursue with very different approaches. 'The multilateral shift adopted by Beijing over the last few years is arguably one of the most salient features of its foreign policy'³⁵. 'China makes a reference to multilateralism in almost

every single policy document it produces'. Although it would not be inaccurate to say that it is to some extent a 'multilateralism with Chinese characteristics', that is to say, marked by a highly selective implication, there is no reason to believe that it is merely rhetorical. 'China's increasing involvement and participation in global and regional multilateral institutions' is undeniable. Such involvement, initially more apparent in economic forums, is now also evident in security institutions³⁶.

China indeed plays an increasingly relevant role in regional and global institutions related to issues such as arms control, regional security, environmental, protection, intellectual property rights and human rights. This is something that the EU clearly supports, as the rising interdependence and the emergence of an increasing number of global problems and issues make it necessary to address them from a concerted framework of shared responsibility, a framework where the Western powers are not the only participants.

Situating multilateralism at the centre of China's 'new diplomacy', Beijing has skillfully managed to create a global web of relations, a fact with important implications for regional and international security³⁷. This multilateral inclination provides China with a good opportunity to improve its international image and be seen as a responsible power. At the same time, it proves that China no longer perceives these institutions as instruments which could eventually be used to punish or constraint it³⁸. They are rather seen as channels through which it can readapt to a wider international community and contribute to the reshaping of the international order as well. China also sees in multilateralism a useful instrument to try to reduce the American preponderance in world affairs, as it might provide a basis to counterbalance such preponderance. Beijing may find support from other regional powers for that strategy³⁹. In brief, multilateralism would be instrumental in the creation of a more multipolar order⁴⁰.

This expansion of multilateralism might seem contradictory in relation to China's strongly held concept of sovereignty. However, it has proved willing to accept certain—however limited—restrictions to its autonomy in the expectation of some benefits and rewards⁴¹. Beijing has concluded that its search of economic modernization, national security and international status will be best served by a strategy of implication in global affairs as well as through an active participation in different forms of institutionalized cooperation. Nevertheless, it is important to note that China uses the term 'multilateralism' in many cases interchangeably with 'multipolarity'. The difference is not a minor one: multilateralism refers to a particular manner of conducting international affairs; multipolarity relates to power distribution. What is more, according to Jian Yang, when the Chinese discuss this issue, 'they use the term 'duojihua', usually translated as 'multipolarity' which, nonetheless should be translated as 'multipolarization''. The difference is again of great importance: China sees multipolarity as something in the making, a process underway which has to be fostered and completed⁴². If we take into account these differences, we can come to the conclusion that whereas the EU is committed to the promotion of multilateralism, what China is really interested in is in promoting multipolarity.

The advancement of multilateralism is in any case a platform where Chinese and EU interests might eventually coincide or, at least, where there is some room to work together, especially in the light of increasing global interdependence in a number of areas. This is possibly the motivation behind the joint commitment to the promotion of an 'effective multilateralism' expressed by China and the EU on the occasion of the EU–China summit held in November 2007⁴³. To make this possible, however, it would be helpful if the EU is seen by China as a relevant political partner.

Human rights are one of the issues which provoke greatest tensions between China and the EU. As has already been mentioned, the views of both actors on this issue are very different, sovereignty usually being the reason given by China in rejecting any foreign criticism, as it considers any comment on 'its human rights practices as an unacceptable interference in its internal affairs'⁴⁴, Chinese reactions to foreign pressure on human rights are clearly conditioned by the very conception of security upheld by the PRC. Beijing assesses security and security threats in terms of the state security level and even the regime's security and not in terms of individual security⁴⁵. Thus, human rights claims may well be considered as threats to national security and as attempts to undermine the Chinese position in the world. In this regard, any questioning of its sovereignty may be seen as a threat to its political security⁴⁶.

One of the most recent bilateral episode of tension as far as human rights are concerned occurred in 2008, when some European countries said that 'they would reconsider their participation in the Olympic Games held in Beijing' if China did not change its stance on human rights and, particularly, its policies on Tibet⁴⁷. The

Chinese, as usual, reacted angrily, as they see such criticisms as Western attempts to intensify the unrest as well as the tensions already observable in these regions⁴⁸. Similarly, in June 2011, in London, Chinese Prime Minister criticized British Prime Minister David Cameron for ‘lecturing Beijing’ in relation with human rights issues. Likewise the Chinese representatives even mentioned that such behaviour might have an impact on bilateral trade relations⁴⁹.

Quite unsurprisingly, the results generated by the EU–China dialogue on human rights—initiated in 1994—which held its last round in Beijing on June 16, 2011, are far from satisfactory. It is little more than a talking shop where little advancement is achieved, something consistent with China’s preferences. Thus, it is broadly felt that, in order to get something relevant out of this dialogue, the EU should try to press for specific advances.⁵⁰

All in all China has shown respect for the UN human rights mechanisms, as proved by its signature of the International Covenants on Civil and Political Rights, and on Economic, Social and Cultural Rights. The PRC even signed in 2005 the UN agreement to protect populations from genocide, war crimes and crimes against humanity. Likewise, over the last few years China is making efforts to reduce torture of suspects and improve criminal procedure legislation and has reduced from 68 to 55 the offenses subjected to death penalty.⁵¹ But this does not change the situation enough, and the European Parliament continues to denounce the Chinese records on these matters, urging Beijing to enforce international norms on human rights so as to guarantee their protection in China. In particular, the EU is concerned with the situation of minorities in Tibet and Xinjiang.

In fact, the recent crackdown on the demonstrations organized in the main cities of China, most likely following the example of the protests in the Arab countries, have proven the concerns of the European Parliament to be right. Thus many cases of detention and beatings—even of foreign journalists—were reported. Similarly, numbers of arrests and extra-judicial disappearances also increased⁵². In this context, it is the arrest and disappearance of Ai Weiwei which has appealed the attention of the general public to a greater extent; however, unfortunately, it is just one example, albeit better known, among many⁵³. That prompted an international response which probably helped to his release, a decision welcomed by Catherine Ashton, High Representative of the EU for Foreign Affairs and Security Policy⁵⁴.

Moreover China’s rigid position may undermine global — and European — efforts to see human rights respected worldwide. Sudan, Zimbabwe, Burma or Syria more recently are paramount examples in this regard. Economic interests seem to prevail, leading Beijing to oppose — and eventually block — any kind of sanction on those countries. This is obviously an area in which Chinese approaches are at odds with Europe’s as it will be considered below when discussing Africa.

5. China’s rise and Europe’s global interests

The increasing importance of the PRC, make it impossible for the EU—or for any other actor in the system—to achieve its goals without taking China into account. China’s rise has already made the PRC a power to be reckoned with and which is often needed if international affairs are to be managed effectively. But this, in turn, requires the PRC to be willing to participate and help to handle the issues in an appropriate manner; it requires the PRC to behave as a ‘responsible international power’.

After thirty years of reform and opening up, China has become an insider in the international system, a power that wants to work to maintain the system. China accepts the values of the international system and acts in support of existing international arrangements⁵⁵. China has certainly flourished under this order. Thus, for example, China has benefited more than any other country from globalization and an open international economy; similarly, by supporting the nuclear non-proliferation treaty, China protects its status as a recognized nuclear power and prevents others from going nuclear.

From a Western perspective, though, China seems in many instances to prioritize its pursuit of short-term national interests, rather than following and shaping global rules, and investing in building international institutions which in the long run—according to the Europeans—would best serve its own interests⁵⁶. A real partnership between the EU and China can only succeed if they work together effectively in international organizations, but when it comes to taking on some of the responsibilities of a leading power, Beijing has held back. China contends more often than not that it remains a developing country which still has a long way to go, and it also sees the main institutions of global governance as being run by Westerners for their own benefit.

At the same time, the manner in which China defines its own security means that what may be considered as responsible behaviour by outside powers may be seen as dangerous for its own security by the PRC⁵⁷. The difference in the Chinese and European approaches helps to explain the tensions which emerge in a number of issues in which the PRC's rise directly affects the EU's positions, such as global governance and climate change, non-proliferation, and Beijing's growing presence on other continents.

5.1. Global governance

The system of global governance is not working. The Copenhagen conference on climate change proved that the UN system is too weak to create effective international energy and carbon emissions control policies. The global trade system is also in deep disarray: the inability to produce a new multilateral trading regime in the Doha round has led instead to regional and bilateral agreements. The G7 has lost its previous relevance and the G20 will be the new platform for securing a consensus among the main powers on trade, finance, and the environment, but it is still in its early stages. There are more and more problems that can only be properly addressed by countries working together and many of the key institutions are working less and less well. The international system needs new frameworks for cooperation or, at least, to find a way to overcome institutional sclerosis.

The EU wants strong global institutions so as to operate within a framework of international law and binding precedents; this is not the case with China. Thus, even if it is undeniable that there is plenty of room for a concerted action between the EU and China on global issues as well as in global frameworks, they have not always managed to concert their positions. They may reach some agreements, as exemplified by the 2004 EU–China Joint Statement on Non-Proliferation and Arms Control or the EU–China Partnership on Climate Change announced at their 2005 annual summit⁵⁸, but disagreements have also frequently emerged—often on those same topics.

International economic institutions must choose between reform and irrelevance. But they cannot be reformed without China's active involvement. The current system of global economic governance does not adequately reflect the rise of China and other emerging economies, while Europe remains over-represented in those institutions, relative to its shrinking share in the global economy. The IMF and the World Bank, created after the Second World War, have to be redefined both to reflect new realities and to increase the representation of those emerging powers. China is getting a larger voting share, a Chinese national has been appointed as the IMF's chief economist, and Beijing is becoming more engaged in debates about development strategies. But China itself is becoming a big lender to the developing world and its unconditional lending to poor countries in Africa and elsewhere may at times undermine sometimes the World Bank's role.

The WTO is seen by developing countries as biased towards the interests of advanced nations, but China has opposed liberalisation plans for agriculture and services. The failure of the Doha round could seriously weaken the WTO and the multilateral trading system, accelerating the proliferation of bilateral deals. As the world's second exporter, China should have an interest in defending the multilateral trading system against the threat of fragmentation.

The G7 has also become unrepresentative and ineffective. Since the early 2000s, their leaders have been inviting selected emerging powers, including China, to their summits. But China was reluctant to participate, defining itself as a developing country, and fearing that this could burden it with more responsibilities for dealing with global economic imbalances, climate change and development issues. Even in the G20, which has replaced the G7 as the institution of reference in the aftermath of the global financial crisis, China has been reluctant to play a leading role in global economic governance issues. The G20 summit in London in April 2009, in which China offered a modest contribution of \$40 billion, demonstrated Beijing's inclination to avoid major burdens.

As one of the largest economies and trading nations, China has also become influential regarding international financial issues. In particular China has gained in particular a new prominence as an international creditor. Its foreign exchange reserves reached \$3 trillion at the end of 2010, and the Chinese government has significantly increased its intergovernmental loans as well as its foreign aid⁵⁹. The strength of China's economy during the global recession has reinforced China's new status in global finance and its willingness to participate in the making of new rules on financial governance.

In early 2009, at the World Economic Forum meeting in Davos, Premier Minister Wen Jiabao stated that ‘the current crisis has fully exposed the deficiencies in the international financial system and its governance structure (...) [There must be] a push for the establishment of a new world economic order that is just, equitable, sound and stable’⁶⁰. As a reflection of this orientation, Beijing has actively promoted international coordination involving the developing countries and, at the same time, has taken steps to promote the use of the RMB in Asia, signing bilateral swap agreements and allowing selected companies in Hong Kong, Shanghai, and Guangdong to settle cross-border transactions in RMB. It has also stepped up its efforts to shape the global policy debate: the boldest move came from the governor of the People’s Bank of China. Zhou Xiaochuan, who in March 2009 joined the debate over the reform of the international monetary system, criticizing the dollar-denominated monetary system and suggesting the creation of a new reserve currency, expanding the role and the composition of Special Drawing Rights.

Such a proposal marked a major departure from China’s traditional approach to global governance. In the words of two analysts, ‘rather than being a rule-taker, China is seeking to be a major rule maker’⁶¹. In fact, however, China’s ability to influence the international financial system remains limited. On the one hand, China is heavily dependent on exports, especially to the United States, which means that it has a vested interest in the stability of the US Dollar. On the other hand, the traditional Chinese notion of national sovereignty makes it hard for Beijing to propose a proper regulatory regime as any global governance arrangement might reduce state sovereignty.

5.2. Climate change

China has been the world’s top producer of greenhouse gases since 2007, overtaking the United States and producing double the emissions of the EU⁶². Although its leaders agree that action must be taken to reduce the country’s emissions, China has pursued an inflexible stance with respect to climate change negotiations. For some authors, there is no area where the room for confrontation and conflict between China and the EU is so great⁶³.

The EU has led efforts to construct a global system for limiting global warming after the Kyoto protocol expires in 2012, conscious that without Chinese participations these efforts are doomed. The Chinese negotiators have argued that it is unfair to compare between different countries ignoring their size in terms of population; and that Western industrial nations, whose greenhouse gas emissions have been building up for more than a century, bear the main historical responsibility for climate change.

Over time, Chinese leaders seem to have recognised the adverse impact that climate change can cause not only in terms of its environmental impact but also its even greater negative economic repercussions, especially on agriculture. China signed the Kyoto Protocol but, as a developing country, it has no quantitative obligations to reduce its emissions. Today, no post-Kyoto system will succeed unless China is part of it. In November 2009 Chinese President Hu Jintao and his American counterpart Barack Obama agreed that a pact was necessary at the Copenhagen UN conference to be held the following month, and that it should include binding emission cuts for developed nations and ‘nationally appropriate’ emission cuts for others.

However, as expected by some, there was an absolute lack of consensus among the leaders. China was at the centre of the discussions in Copenhagen, confirming that it had become the main factor in the negotiations. Beijing was blamed by many as responsible for the failure to agree on legally binding caps on emission levels on which Europeans have insisted so much. Reporters with access to the negotiating sessions have said that China single-handedly blocked a broader deal, opposing a target of 50 per cent reduction in carbon emissions by 2050 and an 80 per cent reduction by developed countries⁶⁴. The final ‘Copenhagen Accord’ was the product of personal negotiations among the political leaders of BASIC (Brazil, South Africa, India and China), meeting subsequently with President Obama, and with the Europeans conspicuously absent. The accord promises a mobilization of \$100 billion in annual funding for developing countries to meet the challenges of climate change from 2020 and also pledges about \$30 billion by 2012 but has no deadline for the finalization of the negotiations and no figures for emission reduction targets by developed nations by 2020.

China had demonstrated great skill in the lead-up to the conference, teaming up with India and other emerging countries to resist the pressures from the industrialized world. From a Chinese viewpoint, the climate change negotiations failed because of the actions and attitudes of the West. Chinese analysts criticize the industrialized

countries and in particular the EU for politicising the climate change negotiations and thus dooming them to failure. They say that, while the EU initially played a pivotal role in setting targets for reducing greenhouse gas emissions, it is now less willing to show leadership in the climate change debate because of its fear of competition from emerging countries and the pressure of conservative policies within the EU⁶⁵.

Climate change thus promises to become a big source of conflict between Brussels and Beijing. The battle to limit carbon emissions will dominate global governance in the coming decades, and the post-Kyoto system will probably need new institutions to make it work. Europe would expect China to be a leader in the shaping of these institutions. Nonetheless, while no doubt climate change is moving up the Chinese political agenda, it is unlikely that China will agree to any climate mitigation action that compromises its national objectives of sustaining economic growth and maintaining social stability⁶⁶. From a European perspective, with regard to climate change, China has displayed that multilateral environmental governance not only is not a priority but is viewed as an obstacle to its freedom of action. Again, China seems to frame the debate over climate change policy as a sovereignty issue.

5.3. Security and non-proliferation

It is interesting to note that, in spite of the circumstances derived from the arms embargo, security cooperation and exchanges between China and the EU exist and are increasingly effective in a number of issues. At this point we have to mention EU exports of civilian technologies which, nonetheless, may be considered as double use technologies, as they have both civil and military uses. In addition, military exercises and other military exchanges between both actors are being held⁶⁷. All in all, it is in the field of new security issues where the cooperation between the EU and China seems to be more relevant.

In this context one must mention the establishment in 1994 of a 'sectoral dialogue' to deal with energy security issues. The dialogue provides a framework in which discuss energy policies and strategies, the evolution of energy markets and the possibilities of securing supplies so as not to endanger sustainable development. This has been an area where cooperation has been particularly successful so far. In 2005 the EU and China signed a MOU on transport and energy strategies which provided the framework for intensified cooperation in areas such as energy regulation, energy efficiency, renewable energy, natural gas and clean coal technology. As far as the latter is concerned, these two parties also launched an Action Plan on Clean Coal in 2005. In the same vein, on the occasion of the EU-China summit held in 2007, both parties insisted on the increasing attention that the issues of energy security, climate change and environmental protection would receive in the framework of the bilateral relation in the years to come⁶⁸.

Cooperation on these issues remains important as competitive dynamics begin to emerge as well. Not in vain, China and the EU are becoming quick developers of wind energy, a sector expected to offer interesting opportunities over the next few decades. All in all, this of wind energy is a sector where EU companies retain the dominant position. The situation is different with solar energy, where China is likely to have the lead⁶⁹.

Partly related to these issues is also the question of non-proliferation and counter proliferation, an area where China is also expected to behave as a responsible power contributing to prevention and reduction of proliferation. Thus, if China could once be considered as a proliferator, over the last few years it has introduced effective controls as far as the export of nuclear related materials and technologies are concerned⁷⁰. However, for many, even if China sees non-proliferation regimes more favourably now than it did in the past, it has not contributed enough towards measures to prevent exports of certain technologies and proliferation⁷¹.

Besides, an area of security which is getting increasingly important and where cooperation between the PRC and the European Union could be really enhanced is that of cyber-security or security for the cyberspace.

5.4. Regional policies

If we look at the ways both actors approach the different regions in the world, the picture is pretty much the same: the EU tries to enforce a number of normative values through mechanisms such as conditionality whereas the PRC is much more guided by pragmatism and self interest⁷².

As mentioned above, if there is an area or issue on the international agenda where European and Chinese approaches are clearly different, it is the case of Africa⁷³. Europe is still the most important foreign actor in the African continent but the Chinese presence is growing quickly. China's presence in Africa is in fact one of the most prominent examples of the go out strategy launched by the PRC in 2001, a strategy aimed at increasing its presence in the developing countries⁷⁴.

The main Chinese leaders have paid numerous visits to Africa over the last few years while affirming that Beijing wanted to establish a 'New Partnership with Africa'⁷⁵. Meanwhile, Chinese business and economic activity in Africa has been fostered by the Export–Import Bank of China and the China Development Bank. These financial institutions have provided Chinese entrepreneurs and investors with loans and investment guarantees of different kinds.

Likewise, in December 2005 the Chinese government adopted its 'Africa White Paper' giving an account of its official 'African policy'. The document outlined the main elements which would shape Chinese cooperation with Africa over the next few years and might also serve as a framework for economic ventures. A step further was taken almost a year later when 48 African leaders attended a meeting in Beijing. On that occasion Hu Jintao announced credits and loans worth several billion dollars and different initiatives to promote Chinese investments in Africa⁷⁶.

The expansion of trade exchanges, which 'have grown at an average annual rate of 33.5 percent' since 2000⁷⁷, the increase of investments and the enhancement of cooperation in the field of human resources with the countries of the region have been especially intense since 2005⁷⁸, suggesting the success of the strategy.

However, rather than trade it is energy that drives Chinese interest in Africa (as in some other regions, too). About a third of the oil imported by China comes from Africa, a proportion which keeps growing. This helps to explain why the oil and mining extractive industries are at the centre of most Chinese economic exchanges with the African continent⁷⁹. 'The construction of a 1,500 km pipeline in Marsha-el-Bashair in Sudan' and the acquisition of 'natural resources extraction rights in countries such as Gabon, the Democratic Republic of Congo and Zimbabwe' are some examples of this⁸⁰.

The leaders of countries such as Sudan or Zimbabwe have welcomed the lack of concern with human rights and democracy shown by China—a lack of concern justified by Beijing in the name of sovereignty and non-interference in the domestic affairs of other states—while they see in the PRC an alternative to the conditionality of the West, the EU of course included⁸¹.

In the light of the Chinese position, even the softer approach developed by the European Union in 2007 on the occasion on the EU–Africa summit, shifting from 'conditionality' to 'political and financial incentives programs' in order to try to foster good governance in the African continent (as is mentioned in the context of the 'Africa–EU strategic partnership 2007') will appear as too demanding at the eyes of the African countries⁸².

All in all, economic benefits may not be the only reason for the active Chinese presence in Africa. The PRC may well have seen in the African countries good partners in its efforts to raise its international profile⁸³. In fact, the Chinese approach to developing nations and African countries in particular might well be seen as a continuation of the path initiated at the 'Afro–Asian People's Solidarity Conference held in Bandung in Indonesia in 1955', and another example of the implementation of the 'five principles of peaceful coexistence'⁸⁴. By the same token some aspects of Chinese anti-colonial and anti-imperial rhetoric and feelings will help its connection with developing countries to some extent. In fact, probably to try to deal with this kind of problem, the European Commission, in its 2006 strategy for Africa, called for a more equal relations with the continent⁸⁵.

Notwithstanding this, Chinese involvement in Africa is not completely problem-free. Thus, over the last few years some voices have started to be heard mentioning that for instances, Chinese mining companies in countries like Zambia and other African countries use old and polluting technologies and machinery, technologies which are even banned by Chinese environmental laws⁸⁶.

In any case, it is clear that European and Chinese approaches are therefore very different. Whereas the European Union tries to get China to support and/or follow its policies against authoritarian governments in the continent and in favor of development, China is much more concerned with its economic and energy interests. Beijing invest large amounts of money, grant loans in very favorable conditions or protect some governments from

international sanctions in exchange for access to their energy resources or particularly beneficial conditions for its companies⁸⁷. Moreover, China criticizes what it considers as 'European hypocrisy': it defends itself by saying that it should not be accused of preventing the improvement of the situation in Africa as Europe has been the dominant actor there for years and the situation has remained unchanged.⁸⁸ In a sense, China cannot avoid feeling that the EU is trying to jeopardize Chinese expansion in Africa.

In an effort to try to deal with these conflicting views and approaches, the European Commission proposed to set up a trilateral dialogue with Africa, China and the EU as participants to try to reconcile the interests of all of them⁸⁹. Similarly, in September 2006, in the context of the EU–China summit, both actors considered convenient to launch a regular dialogue on Africa which might take place at a senior official level⁹⁰, an initiative which was later confirmed by the EU Council in December. Through such cooperation, both could jointly contribute towards fostering growth and development in Africa, an area considered of 'key strategic interest' for both. These dialogues might need to be enlarged to count also include some on other actors with (increasing) interests in the African continent, such as the United States, Brazil, India or Russia⁹¹.

The consolidation of China as a great power over the last decades together with its need to diversify its energy sources have also meant a growing and closer relation between the PRC and the countries in the Middle East⁹². Energy concerns have been the reason for the creation of 'mechanisms such as the China–Arab Cooperation Forum or the China–Gulf Cooperation Council Framework Agreement' aimed at increasing its energy security⁹³.

A case of particular interest is Iran, a country deemed of major significance for China for strategic as well as for economic considerations. In the eyes of Chinese observers, the Islamic Republic is not only a power expected to play an increasingly important role in its region but is also a possible balancing element vis-à-vis the United States and its allies in the Middle East⁹⁴. At the same time Iran is a great source of energy-related products for China. The result is that Sino–Iranian relations have been intensifying, allowing the PRC to become Iran's largest trade partner in 2007. Likewise, China has dramatically increased its investments in Iranian infrastructures.

China is especially interested in the Iranian fossil fuels, as shown by the fact that Iranian oil currently accounts for 15 percent of Chinese total oil imports. In addition, the PRC is negotiating investments in Iranian gas fields worth several billion dollars, it signed a contract worth 1,5 billion dollars to develop several oil projects, and Sinopec will also invest 2,5 billion dollars to upgrade the Arak refinery. In addition Sinopec will also be in charge of the exploration of the Yadavaran gas field, while CNPC (China National Petroleum Corporation) will develop the North and South Azadegan oil fields. For its part, Iran has welcomed this Chinese presence, partly as a tool to counter Western sanctions, and has even invited Chinese experts to advise it in aspects related to economic development.

These policies may be in contradiction of international policies, sanctions and pressures that have been put in place to try to get Iran to fulfill its obligations under the International Atomic Energy Agency (IAEA). While China clearly dislikes the possibility of a nuclear Iran, which would be a serious source of instability in the Middle East and Central Asia, would increase the number of nuclear powers in its neighborhood and would damage the global non-proliferation regime, it also considers that the Iranian right to civilian use of nuclear energy has to be safeguarded, as it is something inherent even to Iran's sovereignty. The PRC would only support sanctions if they are partial and aimed at getting Iran to achieve a negotiated solution to the nuclear issue.

In fact, this is one of the points where the EU and China partially coincide regarding Iran: both have advocated the use of diplomacy and dialogue as instruments to push Tehran to fulfil its international obligations, as well as the importance of achieving a negotiated solution. In this regard the PRC has supported EU efforts (conducted by the 'EU-3': Britain, France and Germany together with the High Representative Javier Solana) to get Iran to abandon its nuclear program through a combination of sanctions and incentives and has even tried to convince Iranian leaders to reciprocate the EU's efforts. In turn, within the framework of their strategic dialogue, the EU has sought to convince the PRC to use its influence on Iran⁹⁵.

Likewise, the PRC is also seeking to develop good relations also with Saudi Arabia as the visit paid by Hu Jintao to the Kingdom seems to suggest. This is not surprising if we take into account that it has also been developing exchanges, deals and investments of different kinds in Saudi Arabia to try to secure the oil coming from this country⁹⁶. It is particularly interesting at this point to stress how, unlike the US, China has managed so far to maintain fluent relations simultaneously with Iran and Saudi Arabia.

Nevertheless energy is not the only element in the exchanges between China and the Middle East as we pointed out above. On the contrary some other aspects such as arms exports have to be taken into account too. In fact, the PRC is one of the many suppliers of the most important military partners for Iran, having developed solid military relations with Iraq, Saudi Arabia or Yemen over different periods in recent history as well. Notwithstanding this, China is also managing to develop increasingly close military relations with Israel which would supply China with military software and related technologies⁹⁷.

In this point, the Chinese reaction to the situation created by the Arab revolutions deserves attention as well. For China the protests could well constitute a threat for its model of cooperative economic relations with non-democratic countries throughout the world. Whereas it may want to preserve its relations with the leaders in those countries, it also has to protect the interests of its own citizens and companies in those countries, which might result badly damaged by both the insecurity as well as a regime change. That dilemma has led China to show a changing and sometimes ambiguous diplomacy over the last few months. Thus, whereas it initially supported the UN Sanctions against Muammar Gaddafi in February, it later on decided 'to abstain on the UN Resolution passed to create a no-fly zone in Libya', a decision much more in line with its vested principle of non interference in internal affairs.

Likewise, in the case of Syria, China also seems to have abided by the non intervention principle.

After all, China cannot discard the possibility of similar events in its own territory and it would like to be free of external interference to deal with them should they take place.

From the point of view of the European Union it is clear that the preferred China is that which supported the sanctions against Gaddafi, the one which might eventually counted on to share costs, burdens and responsibilities in International Crisis Management and not so much the 'traditional' China which stands by the Non Intervention Principle and which constitutes an obstacle for EU's attempts to promote democratic values and good governance worldwide⁹⁸.

The Chinese presence in Latin America is also growing fast, to the point that if this pace continues, it is likely to replace 'the EU as the region's second largest trading partner after the United States'⁹⁹. Thus, China has become one of the main trading partners of Peru, Chile and Brazil and is trying to establish strategic partnerships with some countries in the region. Likewise, almost 50 percent of total Chinese FDI goes to Latin America¹⁰⁰.

In this case, it seems that raw materials in general¹⁰¹, and not merely oil and gas, make Latin America very interesting for China¹⁰². That would have been the reason for a massive increase of Chinese FDI in the production sector in that continent over the last few years. But, as in the case of the Middle East, energy resources are an important factor in the equation: the three biggest Chinese oil companies, CNPC, Sinopec, and CNOOC have reached exploration deals with a number of countries in the region, notably Venezuela, Peru, Ecuador, Argentina and Bolivia¹⁰³.

In the case of Brazil, it is interesting to mention how Baoostel, the largest Chinese steelmaker, invested 1,4 billion dollars in a joint venture with Brazil while the main Chinese companies are working with Petrobras to expand oil production. Likewise, President Lula, in the course of a visit paid to China, expressed his will to build a partnership to integrate the economies of both countries which might be used as an example of South-South co-operation¹⁰⁴.

In the case of Venezuela China has invested more than 400 million dollars in the oil and gas production sectors¹⁰⁵. In exchange, it is trying to secure the long term supply of petroleum. In addition, there are plans for Venezuela to provide Iran with assistance so that it can channel its oil to China¹⁰⁶. In Bolivia, President Evo Morales is also trying to expand its relations with the PRC. He is particularly interested in obtaining Chinese investments in the hydrocarbons sector.

All in all, this growing Chinese presence in Latin America has not benefited all the countries in the region to the same extent. On the contrary, it has increased competition for some countries, notably Mexico, Central America and some Caribbean countries. But Chinese interests in Latin America, at least for the time being, seem to be purely economic and devoid of any political implication. However, as in the case of Africa, the lack of political conditions and the perception of China as an actor which operates outside the 'liberal economic orthodoxy' inherent to the Europeans and the Americans, are very attractive factors for some political leaders in the region¹⁰⁷.

6. Conclusions

China's rise has enormous implications for how the international order is structured and governed. China is now an integral part of the world economy and one of the major winners of globalisation. In joining the world, it has brought about not only changes but also challenges to the existing order. The impact of China's exports, outflow investment and its growing domestic demand are inevitably reshaping the global trade system. Its rapidly growing consumption of energy and raw materials is changing prices and access to these resources. Equally important have proven to be its foreign aid policies and loans. Overall, China's rise has meant an ever growing need for raw materials and natural resources, in order to maintain the pace of growth. This need conditions and often shapes Chinese foreign policy.

As its role in the international economy has grown, so has China's economic relation with Europe. The EU is now China's biggest trade partner and it is this economic dimension of China's rise that has primarily fuelled concern in Europe. While workers fear the transfer of employment to China, and trade unions an unbalanced competition in terms of labour and safety standards, companies are concerned about intellectual property rights and governments about the growing trade deficit with China, in addition to China's growing demand for resources and energy. In many quarters there is the belief that China is the winner of globalisation while Europe will in the longer run loose employment and competitiveness. Against this perspective, there is the fear that China's rise is a major challenge not only to specific European industrial sectors, but even to the EU's social and economic model. Moreover, the EU also sees how China's growing presence in other regions, notably Africa, gradually affects Europe's traditional role as the main partner of such region. This may not only challenge EU economic interests but also undermine its ambitions as a global actor.

China is also a crucial factor in the reform of the institutions of global governance, a matter of great relevance to Europeans. For them, the strengthening of multilateral rules and institutions is a priority. And they see that Beijing has taken an active role in a number of policy areas to defend its expanding national interests and to strengthen its influence in the world. China's position on controversial issues, ranging from human rights to climate change and non-proliferation, shows a readiness to shape global governance according to its own preferences¹⁰⁸. China's leaders seem to have a strong focus on their country's immediate interests, rather than being willing to take on more responsibilities for global governance issues—whether in security or in economic affairs.

This is a demand which puzzles the Chinese, proving the structural asymmetry lying at the heart of the Sino-European relationship. China's foreign policy is predominantly realist, focused on the pursuit of the national interest, while Europeans are driven by rules and the principle of multilateralism. As a consequence, economic governance, climate change, Iran or Africa have become sources of friction in the bilateral relationship. The EU expects China to shoulder more global responsibilities but it is not clear that China is moving into that direction. Aware of its growing capabilities, China seems to prefer an international system based on the balance of power rather than norms and institutions. And yet, China's prosperity and influence—like Europe's—depends on the openness and stability of an international order based on rules.

Ultimately, China is seen as a challenge to the existing world order which was created and defined by the West after the Second World War. With the rise of China (as well as India and other emerging nations) as major new powers on the regional and global level, the Europeans have finally realised that a tectonic shift is taking place in the global balance of power and they are concerned about its effects. But despite the ample space for frictions and misunderstandings, both the EU and China are key players in adapting the international order to these new realities¹⁰⁹.

Even if the single most important geopolitical relationship of the 21st century is likely to be that of China and the United States because of their economic power and potential strategic rivalry, the China-EU relationship will also be indeed crucial. Both sides would therefore benefit from a closer partnership. If China and the EU manage to build a friendly and fruitful strategic partnership they can do a lot to bring about a multilateral world. But if their relation becomes frosty, the scenario of competing blocks will become more plausible¹¹⁰. For these reasons, it is perhaps about time to recognise, as François Godement writes, that '[a] strategic partnership between China and Europe is not designed to limit a strategic competition that does not exist. It is necessary to unlock the potential of each partner along lines of shared interests, with global governance as a goal and respectful debate as the norm'¹¹¹.

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Chapter 7

EU-China political dialogue: looking for a strategic partnership

Alicia Sorroza and Justo Corti

1. A brief introduction to EU-China relations

China started to look towards Europe in the 70s at the same time as its rapprochement with the United States began. Official relations were established in 1975 when Christopher Soames became the first European Commissioner to visit China, and in 1978 the EEC and China signed the first trade agreement¹ which, at the same time established the first Joint Committee.²

Even though during the 80s China encouraged bilateral relations with the big European members (Germany, France and the UK) it was not until the middle of the decade when formal relations were established under the 1985 EC–China Trade and Economic Co–operation Agreement, which continues to be the main legal framework for EU–China relations³.

The 1985 agreement was complemented, in 1994 and 2002, by means of exchanges of letters establishing a broad EU–China political dialogue. However, the development of the relationship was not without its problems during the early period, with China’s rapid economic rise leading to calls for EU protectionism.

The issue of human rights in China has also been present on the Sino–European agenda. The European reaction to the Tiananmen incidents of 4 June 1989 was politically significant. The EC froze its relations with China and imposed a number of sanctions, including an arms embargo that is still in force despite Chinese pressure for its removal.

By the 1990s, the EU–China relationship had significantly altered and expanded with a broader set of dialogues being developed, including a Joint Working Group on Economic and Trade Matters (1993), regular meetings between the EU Troika⁴ and Chinese ministers, and annual EU–China summits since 1998. The decade of the 90s, with the entry into force of the Maastricht Treaty in 1993, was essential in the consolidation of the European integration process, such that China started to realise that the EU was becoming an international actor with influence on the economic and trade sphere and also in the global agenda. However, more than ten years later, it can be said that these expectations have not been reached yet. The EU is not a credible global actor in many areas that it is supposed to be.

In the 2000s, the EU entered in a complex and bittersweet process of institutional reform needed to tackle the many challenges that enlargement and the international context presented in that years. Without going into details, and beyond the nuances that can be done, it is to be hoped that European foreign policy could enter into a new phase, marked by the appointment of the High Representative (HR) and the creation of the European External Action Service (EEAS). However, it is still early to make an overall assessment in this regard and in particular on the EU–China relationship.

2. The two dimensions of Europe-China Relations

The purpose of the following lines is to analyze the two dimensions in the EU–China relationship. Therefore, we will refer to the relations between China and the EU, on the one hand and to the relations between China and EU member states, on the other hand⁵. Trade and economic aspects are mainly carried on by EU institutions⁶. As it is known, the Foreign and Security Policy remains an intergovernmental issue, consequently it is not surprising that some member states, particularly the big ones, try to carry on their own strategy towards China and, at the same time, intent to introduce their national interests in the EU policy. Moreover, inside the EU there are different priorities depending on the institution, which make the developing of a coherent common European strategy even more difficult to achieve.

In this section we will analyse different stresses of policy towards China not only inside the EU but also among the ‘Big Three’ (France, Germany and United Kingdom) and their influence in the Europe–China political dialogue.

2.1. European Commission policy towards China

Until the enter into force of the Lisbon treaty, the European Commission was central in the definition of the EU strategy towards China, taking into consideration that many years ago the EU–China relations were based fundamentally on trade and development issues. Now, with the ‘double hat’ of the HR under the Lisbon Treaty the European Commission has lost the vast majority of its competences on external relations. It just maintains competences on trade and development. However the political and strategic impulse of the Common Foreign and Security Policy (CFSP) is under the HR and the President of the Council, as well as the resources. This is a big difference in comparison with the Pre–Lisbon situation.

A relevant document is the 1995 Communication called ‘A Long Term Policy for China–EU Relations’⁷. This document described China’s progress since 1945. The Commission also emphasised the need for Europe to develop an action–oriented, not a merely declaratory policy, in order to reinforce that relationship. Although the main ideas of this 1995 Communication remained relevant, a number of significant events occurred and gave rise to a need to ‘upgrade’ the EU–China relationship. In this context is important to mention the celebration of the 15th Chinese Communist Party Congress in 1997 where the political Chinese elite expressed its commitment to the market–oriented economy, and to pursue a more responsible role in foreign policy. The successful Hong Kong devolution process, as well as China’s role in the Cambodian peace process, were good examples of this new Chinese approach to the international scene.

In the EU dimension, the single currency and the eastern enlargement gave it new and renewed ambitions in the international level. The Treaty of Amsterdam reinforced its tools and resources within a limited and timid European foreign policy. In this context, the Commission presented in 1998 a second communication on China, which was entitled ‘Building a Comprehensive Partnership with China’⁸.

The new EU–China partnership was expected to engage China through an upgraded political dialogue; however there have been continual concerns, particularly about the respect for human rights and rule of law.

2001 was a turning point in EU–China relations, when both formally declared their intention to forge a strategic partnership. The Commission considered there was a need to deepen Sino–European relations through new communications. The first was entitled ‘EU Strategy towards China: Implementation of the 1998 Communication and Future Steps for a More Effective EU Policy’. There, the Commission suggested ‘ways of developing EU–China relations by defining concrete and practical short and medium term action points for EU policy to progress more effectively towards the long term aims defined in 1998’⁹.

Two years later, the Commission made public another Communication named ‘A Maturing Partnership–Shared Interests and Challenges in EU China Relations (Updating the European Commission’s Communications on EU China Relations of 1998 and 2001)’¹⁰. The Commission recommended the improvement of political dialogue by systematically addressing global and regional governance and security issues. In addition, it emphasised the importance of initiating dialogue and cooperation in the fields of intellectual property rights, sanitary standards, competition policy, industrial policy, among others, and the strengthening of existing dialogues regarding the regulation of industrial products, information society, energy and the environment and technological

cooperation. The reinforcement of the steering role of the EU–China Joint Committee was also proposed, introducing within its tasks a number of sector dialogues.

The EU had undergone a number of changes during these years with the introduction of the Euro, the enlargement, the EU involvement in justice and home affairs related to the fight against international terrorism after 11–S, etc.

In addition, China had emerged as a major player in the world economy. As several authors highlighted in relation to that key moment, a new generation of leaders led Chinese policy and politics, as was observed in the EU–China summit in October 2003¹¹.

Since 2002, Chinese officials noted that the European integration process seemed to be consolidated. Therefore, they found it necessary to devote time and resources to understand and cultivate its relationship with Brussels. In 2003, the Chinese Ministry of Foreign Affairs produced its first policy paper regarding the European Union. The document stated that China was committed to a long–term, stable and full partnership with the EU and that the EU would play an increasingly important role in both regional and international affairs¹². Since the first annual EU–China summit in 1998, the political dialogue was reinforced with an increasing number of meetings in numerous areas. Following this new impetus to EU–China relations, several agreements were signed at the 6th EU–China Summit in October 2003 in Beijing and also in 2004.

Until this moment, Sino–European relations had undergone a convergence process. Some authors described this as a ‘honeymoon period’¹³. The international context dominated by US unilateralism in the global war on terror, mainly with the invasion of Iraq in 2003, led to a rapprochement of positions between some EU member states and China. However, after 2005, EU–China relations began a new phase, more complex and difficult, characterised by several disputes both in the political and in the economic and commercial spheres. The growing European perspective that China is engaging in unfair and opaque trade and business practices has remained as a significant obstacle for stronger EU–China relations¹⁴.

In addition, all the circumstances surrounding the EU arms embargo caused major concern on the part of the Chinese government. Initial moves by the EU Commission to lift the arms embargo failed, because of several factors, but the most relevant were probably US pressures. In addition, the European internal crisis relating to the failure in the ratification process of the EU Constitution caused the Chinese government to rethink the possibility of the EU becoming a real strategic actor in international politics.

At the same time, some events happening in China, such as the Anti–Secession Act (2005) or the non–ratification of the International Covenant on Civil and Political Rights (1966); as well as the evidence that China had already become a global power, have also given impetus to an updated European approach to China.

In this context, the Commission launched the 2006 Communication EU–China ‘Closer Partners, Growing Responsibilities’ that showed a considerable change in EU attitudes towards China¹⁵. It indicated that China had become the world’s fourth largest economy and third exporter, and these facts were translated into a more active and sophisticated Chinese foreign policy. This document also assessed 7 formal Agreements, 22 sectoral dialogues, covering diverse and important issues from aviation and maritime transport to regional and macro–economic policy, describing them as successful and positive. The paper called as well for increased co–operation in science and technology, migration issues, and more effective bilateral structures.

The Commission’s policy paper welcomed the decision at the 9th EU–China Summit (September, 2006) to launch negotiations on a new comprehensive framework agreement. It was supposed that this new agreement would offer a single framework for covering the complexity of the EU–China relationship. Negotiations on a Partnership Cooperation Agreement (PCA) started in January 2007 and are still going on¹⁶.

2.2. European Parliament

It can be said that the European Parliament (EP) has opted for a critical approach to China’s transition to democracy¹⁷. In contrast, the European Commission, and most of the Member States, have maintained during the last decades a more pragmatic and critical position. This different approach can be observed in the various critical Parliament resolutions regarding the record of China’s actions¹⁸.

For example, during the arms embargo affair, the Parliament adopted Resolution P5TA(2003)0599¹⁹ opposing any arms sales to China until there was a significant improvement in human rights respect. The EP has repeatedly mentioned that, regrettably, EU–China relations had only made progress in the trade and economic dimensions, leaving at a subsidiary level the strengthening of human rights and the rule of law. In April 2008, the EP adopted a very critical Resolution as a response to the violent events in Tibet²⁰. In October 2008, the EP awarded the 2008 Sakharov Prize to the human rights activist and Chinese dissident Hu Jia. This event exasperated the Chinese authorities.

The EP President Buzek, on the occasion of the 2010 Nobel Peace Prize granted to the activist Liu Xiaobo, mentioned in a press release that Xiaobo is one of the ‘staunchest defenders of human rights who has fought for the freedom of expression using peaceful means. He stands for the values and fundamental freedoms that the European Union and the European Parliament regard as cornerstones of society²¹. The rest of the European institutions, for example, the President of the European Commission, Barroso, and the High Representative for Foreign and Security Policy, Ashton, at the same time sent their congratulations to Mr. Xiaobo, considering that this prize is ‘a strong message of support to all those around the world who are struggling for freedom and human rights’, but they forgot or failed to mention that he is actually in jail, and to demand the freeing of the activist by the Chinese authorities²².

2.3. EU Members States

Beyond the intention of European institutions, and after the Lisbon Treaty entered into force, it seems that China would have reached the conclusion that Brussels was important for trade and investment issues, but that in foreign and security issues they must continue to talk with France, Germany and the UK²³. There are some many doubts about the role that the European External Action Service will play on these issues.

Since the rise of China as an economic and international power, significant division towards the Asiatic giant have arisen in EU foreign policy.

Economic interests make it very difficult for the EU to develop a coherent and consistent policy towards China. It can be said that the EU member states with significant economic and trade interests in China do not work for a more comprehensive or strong EU foreign policy that could damage or limit their bilateral relations.

Although Member States have different historic ties and philosophies about how to deal with China’s rise, this disunity is increased because EU member states have more to gain from a bilateral approach to China than from an integrated EU policy. In this context, it can be affirmed that this perception is one of the biggest obstacles to a coherent and fruitful EU approach to China.

Several studies have pointed out that the main actors hindering the setting up of a common EU policy towards China are the United Kingdom, France and Germany. Other countries, by contrast, would not be key players in the definition of the EU policy on China²⁴. In general, we can assert that EU Member states are divided over China’s economic impact and its political and human rights development.

Germany

German involvement in China began in the 1700s. Their economic and commercial relationship shows the relevance that German society gives to China. Germany is also China’s largest trading partner in the EU, and its economic interests in China are substantial. The value of Germany’s exports to China in 2010 –53,7 billion–²⁵ was more than three times that of France, almost five times that of Italy, and nearly six times that of the UK.

Traditionally, Germany has criticised China’s politics at the same time as it has defended industrial interests or protected jobs from Chinese unfair competition. Politically, there has been a change in German foreign policy with Angela Merkel’s government. Merkel’s government has given more relevance to human rights than her predecessor Schroeder, who tried to build strong relations with Beijing. The ‘private’ meeting between Chancellor Merkel and the Dalai Lama in September 2007 angered the Chinese government, who decided to cancel several meetings. Consequently Merkel’s government has received strong criticism, especially from the German industrial lobby. Germany could serve as an example of the great difficulties in balancing economic interest with political and ethical issues in relation to China.

United Kingdom

United Kingdom–China ties reflect an important history of relations, with the considerable impact of Hong Kong as crown colony. Until 1984 –when the Sino–British Joint Declaration led to the return of Hong Kong to Chinese sovereignty in 1997– bilateral ties between Beijing and London did not have a real basis on which to build a fruitful relationship, that could be very important for both.

Within Europe, the UK is in favour of allowing Chinese goods to be freely imported into the EU, which is coherent with its commitment to economic liberalism. Britain is the fourth largest European exporter of goods to China and the second in terms of imports of Chinese products. The UK is usually ready to criticize China on political issues, but some recent events seems to show that its traditional focus on human rights could be altered by commercial interests and issues such as climate change. In 2008, the long–standing formal position on Tibet changed, and the UK finally recognised full Chinese sovereignty over this territory.

France

France was one of the first European states to establish diplomatic relations with China in 1964. However, there were several incidents (for example: the sale of military weapons to Taiwan in the 1990s) that produced strong confrontations with China.

Traditionally, France tends to subordinate politics to economic goals, and believes that good political relations will produce economic and commercial benefits. In recent years, Paris has tried to establish a strategic partnership with China. France wants to promote its mutual understanding through different types of events including a high–level diplomatic visit. President Nicolas Sarkozy’s first official visit to China in November 2007 was a great success, and trade agreements were signed. But since then, Sarkozy has adopted a new approach, with open criticism of China’s policy toward Tibet; Sarkozy’s meeting with the Dalai Lama in December 2008, the doubts over his attendance at the inauguration of the Beijing Olympics, among others, are illustrative examples of this policy shift.

As a consequence, China cancelled the Annual EU–China summit of December 2008. According to some officials in Beijing, the decision was taken to let the EU know that there are red lines that should not be crossed and that the Tibet issue is an important one²⁶. However, China acknowledges that France is a swing state in its relations with the EU²⁷.

As is briefly described above, France, Germany and the UK are competing to become China’s more important partner in Europe. They openly criticize the European Commission’s trade position on China, arguing that it is too liberal (France) or too protectionist (United Kingdom and in lesser extent Germany). It can be said that the result of this approach is to undermine EU policy²⁸. The dispute between these three states was very evident regarding whether the EU should lift its arms embargo on China. In that sense, it must be noted that China (as well as other relevant states such as Russia or the United States) has learned to exploit the divisions among EU Member states for its own benefit.

3. Political dialogue on environment, energy and climate change: a little success with some question marks

It is often argued that the EU has difficulties to focus its priorities in Foreign Policy, and particularly in obtaining results. However the EU has been relatively effective in the introduction of the environment’s protection and the climate change as a central issue of the EU–China political dialogue. This is a little story of success of the European diplomacy which, however, still has some question marks.

The EU has a binding unilateral commitment to cut greenhouse gases by at least 20 per cent by 2020 compared with 1990 levels. In addition, the EU aims to achieve a 20 per cent share of renewable energies in overall EU energy consumption by 2020 and, by the same date, its aim is that all member states could obtain a 10 per cent minimum binding target for the share of bio–fuels in transport consumption. However, an important part of the goods and services consumed in the EU produces CO₂ emissions in the exporting countries, particularly in China. Consequently, global objectives of the European Union cannot be achieved without its third country partners, especially when they are important trade partners and, at the same time, big energy consumers such as China.

For this reason the EU is encouraging China to move to a *low carbon economy*.

3.1. First steps

Energy and environmental protection were two of the spheres for which it was agreed to develop economic cooperation in the first Agreement on Trade and Economic Cooperation of 1985²⁹. At this early stage of the political dialogue, the cooperation on energy and environment was included in the comprehensive goal of development of industry and agriculture.

However, it was not until the 1995 European Commission Communication *Long term policy for China and Europe relations* that these spheres of cooperation were developed in specific lines of actions³⁰. The first one was the commitment of EU business and technical expertise 'in a dialogue on the environment, with a transfer of EU expertise in environmental policy-making and technology relevant to Chinese circumstances in key sectors such as energy'³¹. The same document identified as structural problems infrastructure bottlenecks and the environmental degradation risk, both of which could undermine sustainable long term economic growth in China. On the one hand, the European Commission believed that problems of 'acute energy shortages, a transport system which is clearly inefficient and unable to meet demand, and primitive telecommunications, are bound to get worse as economic growth gathers speed and investment in these key sectors lags far behind'³². On the other hand, environmental deterioration was seen as an already serious problem and, despite the government's awareness of the dangers of long-term damage, there was concern that China's economic development strategy was only focused on rapid wealth creation, leaving the consequences to be dealt with for future negotiations. For all these reasons, environmental cooperation was one of the five traditional pillars of EU-China cooperation set out in the 1995 Communication³³.

During the 1990s measures concerning energy and the environment were interlinked with the idea of development cooperation. China still was a developing country and the EU policy on environment and energy in relation to China was conducted through conditions of sustainable development included in aid measures. For example, China was the main beneficiary of the EU's Generalised System of tariff Preferences (GSP), with more than 30% of the value of all beneficiaries' imports in 1997. This scheme integrated non-economic conditions such as international standards of labour rights and environmental protection (International Tropical Timber Organization standards on sustainable management of tropical forests).

Moreover, the EU did not have a policy on energy and the environment specifically designed for China but, by contrast, this was included in the general one for Asia. The 1998 communication *Building a Comprehensive Partnership with China* urged an updating of the objectives of the EU-China cooperation programme in keeping with the reforms and economic growth of China³⁴.

Concerning the environment, there was encouragement of the development of the areas set out in the *Communication on a Europe-Asia Cooperation Strategy in the Field of Environment* (1997), especially cooperation projects focused on clean production methods, waste minimisation, environmental standards, and training and environmental management capacities, as well as appropriate technology transfer³⁵. For the first time, the European Commission introduced greenhouse gas emissions among the priorities. China was no longer a developing country but an emerging industrialized one.

Regarding energy, the 1998 communication also recalled another general document for Europe-Asia, the 1996 Commission's *Communication on a Europe-Asia Cooperation Strategy for Energy*³⁶. The priorities set up in that document were the promotion of energy efficiency and the development of clean coal technologies and alternative energy resources, in particular natural gas. In order to reach these goals, Europe should offer environmental and energy *know-how* and develop synergies with international financing institutions in order to achieve these purposes.

The 1998 communication established the grounds of a Comprehensive Partnership with China and identified the content of the cooperation for the following stage. It clearly interlinked the environment and energy through the common aim of reducing gas emissions, which has become a central element of the EU-China relations in this area.

3.2. The emerge of climate change as a central issue

When the Kyoto Protocol was signed in 1997, China was among the developing nations that did not have any numerical limitation, because they were not main contributors to the greenhouse gas emissions in the pre-treaty industrialization period. However, since then, China has become the largest greenhouse gas emitter³⁷. For this reason climate change has become a central element of the political EU–China dialogue. Even shortly after signing Kyoto, in the *Report from the Commission to the Council and European Parliament on the Implementation of the Communication 'Building a Comprehensive Partnership with China'* (2000), the European Commission described the climate change dialogue as 'a major feature of EU–China relations over the coming years'³⁸. During the implementation of the Comprehensive Partnership Communication of 1998, EU and Chinese experts worked together in studies such as '*Energy Policy and Structure in the People's Republic of China*' (1998), which included priorities for energy policy that were taken into account in the 10th 5-year plan for the period 2001–2005³⁹. On the other hand, meetings of the EC–China Energy Working group explored key areas of cooperation, including cleaner coal, energy efficiency and promoting renewable sources of energy.

In this period China had become the world's second largest consumer of energy and the third largest producer. The impact of the Chinese energy sector was no longer perceived as marginal but as 'a matter of great international importance, particularly for air pollution and climate change'⁴⁰. Estimates of the cost of pollution on the Chinese economy could be as high as 18% of GDP⁴¹. To prevent such harm, on the one hand, the EU offered expert assistance (firstly to control the causes of environmental degradation and secondly, in the medium to longer term, to reverse the harm and to bring about environment improvements). On the other hand, in the 10th 5-year plan, China agreed to increase spending on environmental protection from 0.93% to 1.2% by 2005 and to 1.7% by 2010 (USD 90 billion).

The first EU *Country Strategy Paper: CHINA* (2002–2006) introduced a special strategy for the poorest western regions of China, where 70% of national reserves of minerals are situated and economic structures and the ecological environment are particularly fragile⁴².

The 'Great Western Development Strategy' is conceived as an answer to the imbalance in expansion and a re-adjustment of regional economic structures, especially in favour of the rural economy and its ecology.

For this period (2002–2006) EC financial aid was focused only on three objectives, the most important one being the 'prevention of environmental degradation; conservation of the natural environment; and the integration of environmental considerations into other policy areas...', particularly in western areas⁴³. Concerning interactions between energy and the environment, the paper focuses on the promotion of energy efficiency, as well as on transferring energy technologies, e.g. clean coal, natural gas, nuclear fission, and alternative energy technologies, notably in the fields of new and renewable energies.

However, actions linked to the environment (Priority 2: Environment and Sustainable Development) were funded only with 45 million Euros, clearly an insufficient amount for all the goals expected.

In the 2003 document the European Commission recognised, for the first time, the central role of China as a global player in environmental aspects⁴⁴. The EU and China have 'shared responsibilities in promoting global governance', particularly 'on global environmental challenges, including enhanced cooperation on the Kyoto protocol and climate change, and on follow-up to the World Summit on Sustainable Development'⁴⁵. China is not just a developing country towards which the EU provides financial and technical support on environmental issues but also an equal partner that plays a leading role in the global environmental arena.

In this connection, the *Joint Declaration on Climate Change between China and the European Union* (2005) fixed two cooperation goals by 2020 for climate change⁴⁶. The first one is the support of clean coal technologies, mainly through carbon capture and storage. The second is the promotion of energy efficiency and renewable energies. Taking into account that 70 percent of Chinese energy consumption comes from coal, it is clear that carbon capture and storage initiatives are a key element of cooperation.

The 2006 communication, *EU–China: closer partners, growing responsibilities*, introduced onto the agenda European concerns about the rapid growth of China's demand for energy and raw materials in international markets⁴⁷. It was clear that China's development could have an environmental impact not only inside its own boundaries but also in third countries, particularly exporters of raw materials in Africa and Latin America.

For that reason the EU, on one hand, offered to ensure China's integration into the world energy market and, on the other hand, encouraged China to become an active and responsible energy partner. This partnership should include the improvement of security in exporting countries, including African countries⁴⁸, as well as the reinforcing of bilateral and international cooperation under the Climate Change Convention and Kyoto Protocol, particularly in the dialogues on international climate change co-operation post-2012.

In the same year, in its conclusions on the *EU–China Strategic Partnership*, the Council reaffirmed the strategic interest in China–Africa cooperation and the Near Zero–Emissions Coal technology⁴⁹. Concerning the reinforcement of international environmental governance, the council asked for Chinese support in the possible transformation of United Nations Environment Programme (UNEP) into a UN agency for environment, recognising its important role as a global player.

In the last *Country Strategy Paper 2007–13*, the European Commission confirmed all the objectives already described in previous documents, but introduced a specific goal related to the flagship Near Zero Emissions Coal Project (NZEC): to develop a NZEC demonstration plant with carbon capture and storage in China by 2020⁵⁰.

In response to these initiatives, in 2007 China established a National Leading Group on Climate Change that developed a programme centred on energy efficiency, renewable energies and reforestation⁵¹. In 2008 the Chinese government published a white paper on *China's policies and actions on climate change*⁵². In this document China recognized that climate change has brought substantial threats to the natural ecosystems as well as to the economic and social development of the country. However, as support for China's individual vision, its 2007 *National Plan for Coping with Climate Change* cites the 'historical responsibilities' of industrialized countries, in conjunction with the principle of 'common but differentiated responsibilities'⁵³ of the UNFCCC (United Nations Framework Convention on Climate Change), and its relatively low-ranking position among countries' per capita emissions. Concerning the control of greenhouse gas emissions, this plan includes a target of about 20% reduction of energy consumption per unit GDP by 2010 compared to that of 2005; a rise of the proportion of renewable energy (including hydropower) by 10 percent for 2010; the freezing of the emissions of nitrous oxide from industrial production at 2005 levels and an increase by 20 percent of forest coverage rate by 2010 from 2005 levels. These objectives were welcome but they are so ambitious and the periods of implementation so short that they seem very difficult to achieve.

In the *Copenhagen Conference* China did not support EU objectives⁵⁴. The final agreement, drafted by the US, China, India, Brazil and South Africa, recognises the scientific case for keeping temperature rises below 2°C, but does not contain commitments for reduced emissions that would be necessary to achieve that aim. However in February 2010, China, confirming its voluntary commitments under the Copenhagen Accord, declared its intention to lower its carbon dioxide emissions per unit of GDP by 40–45% by 2020 compared to the 2005 level; to increase the share of non-fossil fuels in primary energy consumption to around 15% by 2020; and to increase forest coverage by 40 million hectares and forest stock volume by 1.3 billion cubic metres by 2020 from 2005 levels⁵⁵. The first analysis on the *Durban Conference* insinuates that things would not be very different⁵⁶.

Although the achievement of the European diplomacy in putting the environmental issue on the Chinese agenda, it seems that things are changing rapidly. The new context of the financial crisis is reducing the power of bargain of Europe and, for the first time, the question is not how to influence China but how to reduce the increasing power of China in writing European Foreign Policy.

4. China's relevance in a never-ending financial crisis: a new puzzle of interest within EU

The map of European–Sino relations described above is rapidly changing in a context of a deep and severe crisis of the EU, especially for the Eurozone.

It is well known the excellent (but also with a stormy horizon in the future) economic performance of the also called emerging (emerged could be more exact) countries or powers during this international economic crisis. In this context, we want to reinforce the idea that China will be a relevant partner for the EU, but also the opposite, the EU market for China will still be significant for the Chinese products.

As Bustelo noted, in recent years, China has been the true engine of the world economy even more than other larger economies⁵⁷. China as the others emerging countries, in the current international financial crisis, has the 'cash' that the rest of the developed economies need these days. And China knows and exploits these advantages. A recent piece of analysis argues some kind of a 'scramble for Europe'. The authors stress that 'China is buying up Europe'⁵⁸. Maybe this declaration is a bit exaggerated. However it is a fact that Europe needs China and welcomes its presence. On one hand, the EU needs to improve market confidence in public debt, to save companies and jobs. On the other hand, China seems willing to invest in Europe, especially in peripheral countries.

China is also purchasing public debt (or announced it) in peripherals EU member's states and it uses this readiness as a tool for public diplomacy⁵⁹.

China seems to have understood that it needs closer ties and has to be more influential in Europe if it wants to improve its access to European markets through others channels⁶⁰. China is taking advantage of this critical juncture and it is launching a strategy already applied in developing countries.

As it is known, during the past years China has focused on outbound investment in Asia and in other developing regions, like Africa and South America. Europe has hardly seen any activity whether in merger and acquisition (M&A), bank loans or trade & cooperation agreements. Clearly, this has changed.

According to the Grisons Peak China Outbound Investment research report, this tendency has changed during the past months. Chinese investment in Europe, and especially in Mediterranean countries, has grown significantly. In 2009 the first major trade agreement with Germany was signed, meanwhile Bank loans, with a focus on Mediterranean Europe, were granted in the second semester of that year. During 2010 there was a significant increase in merger and acquisitions and equity investment across Europe. The European Mediterranean countries were the chosen partners of numerous Trade Agreements and this tendency has continued throughout 2011. Mediterranean countries represent approximately 30% of total Chinese investments in Europe, a very important average considering the size of these economies⁶¹.

According to an recent report, Chinese companies are preparing for a wave of new investments in Europe in engineering and technology as part of an effort to find new markets and gain greater control of global supply chains⁶².

In accordance with the same source, Chinese investments in the last quarter of 2010 and the first quarter of 2011 reached \$64.3bn. This is more than double that the previous 11 ones. According to banking experts, many Chinese companies see European deals as a 'short cut to a customer base'. China's presence in Europe creates many problems in terms of competition, mainly because this direct investment is made by Chinese state-owned companies that may (or not) receive large subsidies⁶³. The lack of transparency is usually the rule. It has also opened a debate in EU about the need to establish a vetting process of direct foreign investment especially in areas that are considered strategic.

As it is mention before, since the eurozone debt crisis broke out in 2010, China has been buying bond from southern member states as Greece, Portugal and Spain, and also made promises to the Irish and Hungarian government⁶⁴. However, we must be cautious with this numbers, because China only publishes its total currency reserves, and not the composition by country. In addition, Europe does not publishes aggregate data on foreign purchasers of public debt of their EU member states.

This opacity and lack of transparency allow a sort of financial 'game of blind poker'⁶⁵, whose main beneficiary is China, whose intentions and potential capabilities are often overestimated, and it could also produce a competition between EU member states for attracting Chinese sovereign funds, making an EU coherent policy towards China more difficult. Beyond the actual data (or lack of it) regarding the bonds, China's strategy seems to be quite clear about this. China is gaining influence in Europe to strengthen ties and has greater interest in some European countries in order to reduce its exposure to the U.S. economy. According to Chinese authorities, the counterpart that China searches, beyond the benefits of its investments, is related, on one hand, to the advantage of obtaining the status of a market economy earlier than expected and, on the other hand, to the reduction of the current pressure on the appreciation of the renminbi. Others issues as the arms embargo lift and the human rights issue are also being mentioned, but they seem to be less important. Speaking at the opening of a three-day summer session of the World Economic Forum in the Chinese port city of Dalian, the 14 September 2011, Chinese Premier Wen Jiabao said China would continue to expand its investment in Europe.

Wen said that EU and major European leaders should consider their relations with China from a strategic point of view. Despite the World Trade Organization's intent to give to China full market economy status in 2016, Wen said that European nations could demonstrate their sincerity and friendship by according China the full status several years earlier. As it is largely described in others chapters in this book, and mentioned in this document, China is constantly demanding that EU grants the full market status to Chinese economy. For the EU, and despite the economic concerns over the lack of transparency in several sectors of Chinese market, the access to the EU market is a tool for pressing Chinese authorities in order to obtain European claims regarding China's market access for European companies⁶⁶.

Despite the difficulties to compare data on the real dimension of China's presence in European countries, we can see a change in the Chinese approach to the EU and particularly to some European countries, especially eastern and southern peripheral regions. These countries that until a couple of years ago did not have any relevant interests in China are following UK, Germany and France in the design of EU policy towards China.

A good number of these countries now seek to draw the attention of the Asian giant in terms of investment and the purchase of debt as a tool to overcome the crisis, without greater demands on human rights issues or in the improvement of the access to the Chinese market.

China has focused on Europe, and is using all the tools at its disposal to be not just as a mere trading partner. This new Chinese approach, essentially bilateral, but expanded to other countries beyond their traditional European partners, can positively influence the interest of European leaders of the main EU member states, to strengthen the EU dimension in their relationship with China. It is becoming clearer that without a clear policy it will be very difficult to press China to improve conditions for market access, prevent dumping, and so on.

However, in practical terms, the reality is that new interests and actors are on the negotiation table, so it will surely be more difficult to reach a European consensus (EU policy) on this matter⁶⁷.

Both sides, China and Europe, pretend to maximize profits. China, of course, acts motivated by its economic and political interests. But the European members states should act differently, they should assume that they need to agree a common position to address the challenges posed by China in economic and political issues.

5. Conclusions

Relations between the EU and China have developed rapidly in recent years. However, there are several controversial areas such as human rights respect, the arms embargo, the trade imbalance, market economy status (MES), currency levels and intellectual property rights (IPR), where it has not been possible to achieve intra EU consensus. European division has led to a lack of a clear political impulse in the EU policy toward China.

Within this context, the EU has focused its diplomatic efforts on the construction of an institutionalised framework, characterised by a number of meetings, summits, dialogues, cooperation projects, and so on. Increasing contact has helped to enhanced understanding, but there remain considerable misperceptions. Difficulties of reaching a partnership and a cooperation agreement show the limits of this approach and the need to change it.

It is true that many examples of very good cooperation beyond trade and investment can be found, such as on clean coal technology, or even some kind of European influence in the Chinese environmental policy, for instance on climate change. However these cases are marginal and the final results of the influence of the EU in the Chinese internal or international policy have many question marks.

Moreover, the role of the EU in the incorporation of China in the trade economy (including trade and investment flows) could not be qualified as a real policy but a consequence of China's successful economic model⁶⁸.

This conclusion is really worrying, since as it was reaffirmed in several chapters of this book, the only aspect with regard to which the EU has enough weight and scope is in trade and economic issues. Even in environmental issues, the case explained in this chapter, during last years the EU has been losing leadership⁶⁹.

The two main weakness of EU policy towards China are, on one hand, the lack of coordination between the EU institutions and main member states in their policies and, on the other hand, the absence of a clear EU leadership in the conformation of an European policy toward China (EU plus member states).

On the first issue, the EU has to understand that commercial partnership does not automatically translate into stronger political ties. For this reason, it is fundamental for the future of the EU–China relationship that the so-called big three (Germany, France and the United Kingdom) agree to pool their efforts and strongly support the EU’s position towards China.

On the second issue, the creation of the European External Service is supposed to be a promising tool for creating real EU leadership. For example, Ms Ashton, following a Van Rompuy’s initiative, declared the strategic partnerships to be one of her main priorities for 2010 and beyond. We have entered in a post–Lisbon era, maybe it is still early to know whether this new attempt will give the expected results, but regrettably it seems that this initiative has lost impulse during the last months. The big question is whether the international scenario will give us the time that we need for implementing the Lisbon treaty.

It is very difficult to try to ‘predict’ what kind of international arena we will have in the next few years. International experts speculate about multilateralism, an inter-polar or a multipolar world⁷⁰. Despite these uncertainties, there are some facts that cannot be contested. The financial and economic crisis has accelerated a series of changes in the international scenario reducing the power of the traditional transatlantic pole, and the emergence of the East and South actors. There seems to be a lack of ability in the EU to make a critical assessment of this new geopolitical context and turn it into lessons learned, in order to guide a change in its attitude towards new actors, like China.

If the EU cannot achieve a coherent policy towards China on time, maybe it will not have enough influence to carry it on.

In this sense, the EU has to realise that nowadays the EU and China compete for obtaining raw materials and markets in same regions of the world, particularly in Africa and Latin America. Consequently the EU policy towards China does not only involve the EU and China, but also third countries. With the risk of simplifying the complexity of Chinese foreign policy, there are some elements that must be remarked. On the one hand, the uncompromising defence of the principle of ‘One China’, including the full respect of its territorial integrity and sovereignty, without any exception. On the other hand, the Chinese regime needs to maintain the development process and economic growth. The economic and social development is perceived as essential to the sustainability of the Chinese political regime, structured around the Chinese Communist Party (CCP)⁷¹. The base of legitimacy of Chinese leadership has little to do with communism (and the class struggle) and much more with the improvement of the living conditions of millions of Chinese citizens. Therefore, the Chinese Communist Party articulates the priorities of Chinese foreign policy to meet their national targets for economic and social development. This is, and will remain, at least in the medium term, the driving force behind China’s external action, therefore any European action in this area must take into account these two elements and not create high expectations about the possibility that China might accept any crossing of this red lines.

However, the EU still has important tools to bargain. In this context, it is also essential to highlight what China specifically seeks in the EU. Here we must mention two main issues highlighted by a number of European and Chinese analysts. The first is the market economy status recognition by European countries.⁷² Currently, the MES is a political instrument used to pressure the Chinese government in other matters, such as the need to appreciate the renminbi, among others.

The second is the EU arms embargo that was imposed on China following the events in Tiananmen Square. As recognised by a number of reports, the embargo is not a conventional one, it is not legally binding, and each country applies it in a different manner. The EU arms embargo is perceived by the Chinese authorities as a humiliation, because they are treated in the same way as Sudan or Zimbabwe. Likewise, on the European side, it is considered as an instrument for putting pressure on China in relation to human rights and the scope of the rule of law, and is a very sensitive issue in European relations with other partners such as United States or Japan.

Finally, it is recognised that the EU–China dialogues are strategically important, but this does not automatically translate to Strategic Partnership as pretended. The so called ‘strategic partnership’ is not strategic in a strict sense of the word. Regrettably, despite some consensus between China and EU on several issues there are many differences that cannot be under-valuated. There is no doubt that the global challenges that we are facing need strong and solid ties with China (and other international powers). We believe that the EU institutions, together with the Member States cannot delay rethinking their approach and their strategy towards China.

6. Endnotes

- 1 See the Council Regulation (EEC) 946/78. The two main clauses of this agreement are the most-favoured-nation treatment (art. 2) and the balance in trade attainment (art.3). According to the last one, if and obvious imbalance arise, the matter must be examined within the Joint Committee so that measures can be recommended in order to improve the situation.
- 2 The Committee established by art. 9 of the agreement has competences on trade relations only, for example 'to examine means and new opportunities of developing trade between the Contracting Parties and other problems relating to their trade', particularly the correction of the imbalance in trade.
- 3 Council Regulation (EEC) 2616/85 of 16 September 1985 concerning the conclusion of a Trade and Economic Cooperation Agreement between the European Economic Community and the People's Republic of China, p.1.
- 4 In the EU context before the entry into force of the Lisbon Treaty, 'troika' refers to the trinity comprising the member state holding the Presidency of the Council, the Member State which had held the Presidency in the previous six months and the Member State which would be holding the Presidency in the next six months.
- 5 There could be a third dimension (transnational companies, NGOs, trade unions, etc.). However neither in EU documents nor China ones it is enough developed the role of these stakeholders yet. On this regards see Liu Fei 2007, p. 120.
- 6 There are exceptions, for example issues concerning foreign direct investment (FDI). On this regards, see in this book the chapter of Jeremy Clegg & Hinrich Voss.
- 7 European Commission, 1995.
- 8 European Commission, 1998.
- 9 European Commission, 2001, p.3.
- 10 European Commission, 2003.
- 11 Cameron, F., 2009, p.52; Gill B. and M. Murphy, 2008, p.4.
- 12 People's Republic of China, 2003.
- 13 Gill, B. and M. Murphy 2008, p.30.
- 14 On this regards see the chapters of Enrique Fanjul and Jerónimo Maillo.
- 15 European Commission, 2006.
- 16 Concerning the main issues of these negotiations see Zeng, L., 2009.
- 17 Cameron, F., 2009, p. 57.
- 18 In its Resolution of February 2001, the EP called on China to guarantee the constitutional right to freedom of religion and belief, together with the exercise of the associated rights of freedom of conscience, freedom of expression, freedom of association and freedom of assembly.
- 19 EP Resolution P5_TA (2003)0599 available at <http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P5-TA-2003-0599&language=EN> (accessed on 5 December 2011).
- 20 EP Resolution P6_TA(2008)0119 available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:2009:247E:0005:0007:EN:PDF> (accessed on 5 December 2011)
- 21 The press release is available at the EP web site: <http://www.europarl.europa.eu/es/pressroom/content/20101008IPR86243>, (accessed 5 December 2011).
- 22 Barroso's message to Mr. Liu Xiabo, available at http://ec.europa.eu/commission_2010-2014/president/news/speeches-statements/2010/10/20101008_speeches_2_en.htm, (accessed 5 December 2011).

- 23 House of Lords, 2010, p 20.
- 24 Rees, N. 2009, pp. 31–46.; Fox, J and F. Godement 2009.
- 25 Federal Republic of Germany, 2011, p. 2.
- 26 Brown, K. and S. Crossick 2009, p. 5.
- 27 For a broader analysis of EU–27 Member states’ attitudes towards China, consult Fox, J. and F. Godement 2009.
- 28 Brown, K. and S. Crossick 2009, p. 6. Fox, J. and F. Godement 2009, p. 24. Grant, C and K. Barysh 2008.
- 29 Agreement on Trade and Economic Cooperation between the European Economic Community and the People’s Republic of China, art. 10.
- 30 European Commission, 1995.
- 31 European Commission, 1995, p. 16.
- 32 European Commission, 1995, p. 21.
- 33 The others were human resources development, administrative and social reforms, business and industrial cooperation, rural and urban poverty alleviation.
- 34 European Commission, 1998.
- 35 European Commission, 1997.
- 36 European Commission, 1996.
- 37 With 215% of total emissions according to the UN statistics division. See United Nations ‘Millennium Development Goals Report 2011’ available at http://www.un.org/millenniumgoals/11_MDG%20Report_EN.pdf (accessed on 5 December 2011)
- 38 European Commission, 2001.
- 39 Andrews–Speed, P. et al. 1999.
- 40 European Commission, 2001.
- 41 Smil V. and M. Yushi, 1998.
- 42 Commission Working Document Country Strategy Paper: China (2002–2006) available at http://ec.europa.eu/external_relations/china/csp/02_06_en.pdf (accessed on 5 December 2011)
- 43 These objectives are (1) Support for the social and economic reform process to ensure sustainable economic development and the fight against poverty, and China’s integration in the world economy, with special emphasis on WTO implementation; (2) Prevention of environmental degradation; conservation of the natural environment, integration of environmental considerations into other policy areas, actions to pursue improved balance between environmental protection and social development in the context of rapid economic growth and (3) Support for the transition to an open society based on the rule of law and respect of human rights, through the promotion of good governance and democracy and human rights–related policies.
- 44 European Commission, 2003.
- 45 European Commission, 2003, p. 12.
- 46 Joint Declaration on Climate Change between China and the European Union Brussels, 7 September 2005, 12009/05 (Presse 226).
- 47 European Commission, 2006.

- 48 Concerning Africa, according to the document, 'The EU and China should engage in a structured dialogue on Africa's sustainable development. There should be transparency on the activity and priorities of both sides, providing a basis for full discussion; support regional efforts to improve governance in Africa; [and] explore opportunities for improving China's integration into international efforts to improve aid efficiency, co-ordination and opportunities for practical bilateral co-operation on the ground.' European Commission, 2006, p. 6.
- 49 Conclusions on the EU–China Strategic Partnership, 2771st Council Meeting General Affairs and External Relations, Brussels, 11–12 December 2006, Press Release 16291/06 (Presse 353).
- 50 Commission Working Document Country Strategy Paper: China (2007–2013), available on http://ec.europa.eu/external_relations/china/csp/07_13_en.pdf (accessed on 5 December 2011). The EU–China Near Zero Emissions Coal (NZEC) agreement was signed at the EU–China Summit under the UK's presidency of the EU (2005) in the context of the EU–China Partnership on Climate Change. The aim is to create a NZEC technology economically viable through CCS (CO₂ Capture and Storage) by 2020. The NZEC initiative is working hand-in-hand with the COACH project (Cooperation Action within CCS China–EU), an EU funded project under the 6th Framework Programme that aims to prepare the ground for implementation in China of large-scale energy facilities with options for coal-based electric power generation as well as the production of hydrogen and synthetic fuels.
- 51 Chinese Government, 2007.
- 52 An official English version is available at: http://www.china.org.cn/government/news/2008-10/29/content_16681689.htm (accessed 5 December 2011).
- 53 Chinese Government, 2007, p. 2
- 54 These objectives addressed three key challenges: targets and actions; financing [of low-carbon development and adaptation]; and building an effective global carbon market. See European Commission 2009.
- 55 Fox, J. and F. Godement, 2009.
- 56 Fuentes–Bracamontes, R., 2011.
- 57 Bustelo, P. 2011.
- 58 Godement F, and J. Parello–Plesner, 2011, p. 1.
- 59 Foreign Policy Association, 2011.
- 60 Concerning the access of China to European markets as Foreign Direct investor see in this book the chapter of Jeremy Clegg and Hinrich Voss.
- 61 Grisons Peak Merchant Bank, 2011.
- 62 Financial Times, 2011. Available at <http://cachef.ft.com/cms/s/0/a9662ca0-6f59-11e0-952c-00144feabdc0.html#axzz1bt1f6l4s> (accessed 28 November 2011)
- 63 Regarding the treatment that European companies are receiving in China see the chapter of Jerónimo Maillo.
- 64 The Economist, 2011, available at <http://www.economist.com/node/18895430> (accessed. 28 November 2011).
- 65 Godement F, and J. Parello–Plesner, 2011, p 4.
- 66 See for example, Orlik, T., 2011.
- 67 For some academics, (see, for example chapter 5 written by Zhimin Chen this is an opportunity to reinforce the EU–China relations, based on strong bilateral relations.
- 68 Ludow, P. 2007, pp.14.

- 69 European Union was marginalized from the final agreement in the past Copenhagen summit in December 2009.
- 70 On this regards see chapter 1, written by Mario Telò and chapter 2, written by Juliet Lodge and Angela Carpenter.
- 71 See Xinning Song chapter on this book.
- 72 House of Lords, 2010, p 48.

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Chapter 8

Bilateral trade relations and business cooperation

Enrique Fanjul

1. Introduction

The aim of this chapter is to analyze trade and business cooperation between the EU and China, in order to make proposals for improving and expanding such trade and cooperation in the future. The paper mainly focuses on issues and questions that have achieved a particular prominence in recent times.

The chapter is divided into three major parts.

In the first part we review the environment for trade and business relations. We address three issues that have gained special relevance:

- The uncertainties about the business climate for foreign companies, which have increased significantly in recent months, darkening the perception of the Chinese market among many European companies.
- The main irritants in bilateral trade. In this section we consider three issues: the EU trade deficit with China, EU protectionist measures against Chinese products, and the question of the exchange rate of the Chinese currency.
- Changes in the pattern of growth of the Chinese economy, which involve changes in business opportunities for European companies.

The second part is aimed at analyzing problems of access to the Chinese market. We discuss a number of issues: regulations, certifications, foreign investment restrictions, etc., with particular attention to restrictions that have recently emerged – such as the new policy favouring ‘indigenous innovation’ in public procurement.

The third and last part contains some conclusions and identifies several windows of opportunity for the future in trade relations and business cooperation between the EU and China. We make some recommendations or suggestions to encourage greater use of these opportunities.

2. The environment for trade and business

2.1. Uncertainties on the business climate in China

In recent times many companies and business organisations have perceived a significant deterioration in the business climate in China for foreign companies. It is too early to make a precise assessment of the subject, but many foreign companies, including European companies, are concerned about what they perceive as worsening conditions for the conduct of their activities in the Chinese market.

What is new in comparison with former times is that, since 2009, companies started to voice their discontent openly. In the past companies used to maintain a low profile in order to avoid angering Chinese authorities and suffering subsequent retaliation.

An important qualification is that complaints mainly affect technology-based, machinery and services companies, etc. Consumer goods companies face a much more favourable situation. For these companies, China has become a booming market. In the fields of luxury consumer goods, China is one of the world's most dynamic markets, and for many major international brands this has been a real lifeline in recent times of economic crisis.

Numerous reports in the press and from relevant institutions have pointed to this deterioration. James McGregor, former president of the American Chamber of Commerce in China, noted in the pages of *Time* magazine that

'In more than two decades in China, I have seldom seen the foreign business community more angry and disillusioned than it is today (...) Anti-foreign attitudes and policies in China have been growing and hardening since the global economic crisis pushed the U.S. and Europe into a tailspin and launched China to its very uncomfortable stardom on the world stage. (...) CEOs' banquet-table chatter is now dominated by swapping tales of arrogant and insolent Chinese bureaucrats and business partners. The litany includes purposefully inconsistent and non-transparent enforcement of regulations, rampant intellectual-property theft, state penetration of multinationals through union and Communist Party organizations, blatant market impediments through rigged product standards and testing, politicized courts and agencies that almost always favor local companies, creative and selective enforcement of WTO requirements ... The list goes on'¹.

In 2009, the European Union Chamber of Commerce in China issued an important Position Paper that conducted a thorough analysis of the conditions for business. The report carried out a detailed review of the growing number of obstacles facing European companies for the development of their activities in China. In its Executive Summary, the European Chamber of Commerce summarized in a very clear way the concerns about this deterioration: 'Right across industries, European businesses are still impeded by issues concerning market access, legal and political transparency and the protection of Intellectual Property Rights (IPR). The spectre of protectionism has also appeared, and European companies are increasingly concerned by the tendency for local companies to be favoured over foreign-invested ones'².

'The Chinese authorities should not take the presence and commitment of European companies for granted,' said Jacques de Boisseson, president of the European Chamber of Commerce in China, at the end of June 2010. 'This massive commitment to the Chinese market is not unconditional. If perceived risks materialise to a great extent, the presence and commitment of our members may disappear'³. Mr. Boisseson was speaking at the launch of the chamber's annual survey of European businesses in China. According to this survey, 64% of companies said China was one of their top three destinations for investment. But 39% of European companies said they expected the regulatory environment would worsen over the next two years, with only 10% expecting an improvement.

Leading representatives of companies have raised their voices to present their concern over developments in the business climate in China. BASF's chairman and the chief executive of Siemens made statements almost simultaneously in July 2010, criticizing the restrictions on foreign investment in many sectors and the obligations on technology transfer that the authorities imposed on foreign companies⁴.

These concerns were reflected in one of the more important publications about the business climate in China, the *Business Climate Survey 2010*, prepared by the American Chamber of Commerce in China. In the introduction to the study, the chairman of the Chamber wrote:

'This year's findings show the complex challenges facing the US business community in China. While most American companies are doing well in China, they are concurrently troubled by a mounting number of policy challenges ranging from the inconsistent enforcement of laws, to China's discriminatory domestic innovation policies and regulations that limit market access into sectors that had been increasingly open to foreign investment for the past 30 years. These policies appear to be diminishing the ability of foreign companies to access the Chinese domestic market, right at a time China is shifting from being an export-led economy to a more domestic-consumption-led economy.'⁵

According to the study, based on a survey among US companies, they are becoming increasingly concerned with inconsistent regulatory implementation, which they rated as their most significant challenge for the first time on record.

Some particular conflicts, which have had a major impact, have particularly contributed to this deterioration in the perception of business within China. The conflict that has had the greatest media impact was probably that of Google. Another conflict that has generated a strong concern is the case of the four employees of the mining company Rio Tinto formally arrested and charged with receiving bribes. The four employees were sentenced to jail terms, but no bribe payer has been prosecuted.

This arrest raised concern among foreign companies operating in China regarding the status of their employees and the alleged use by the Chinese authorities of intimidating practices in relation to trade negotiations. According to media reports, the arrests came shortly after serious disagreements between Chinese companies and the Australian mining company. These included the rejection by Rio Tinto of a proposed investment by Chinalco, a Chinese state company in the aluminium industry, and the lack of agreement on the sale price of iron ore to Chinese buyers.

The last judicial cases of dispute have cast a shadow over the evolution of the legal system in the P. R. China. According to Jerome Cohen (co-director of the Asia Law Institute at the University of New York), and Yu-Jie Chen, a researcher at the Asia Law Institute,

‘Despite continuing grave violations of existing international standards for protecting civil and political rights, China’s overall direction in international law, at least until recently, has seemed progressive. Now, however, an old, nationalistic tone has begun to mark its criminal prosecutions of foreigners as well as of Chinese dissidents, often explained with vague references to ‘judicial sovereignty’ without further elucidation. This may reflect the setbacks that China’s domestic criminal justice system has suffered since the 17th Communist Party Congress introduced tougher policies and personnel in late 2007. It may also reflect a change in the Chinese government’s attitude towards international law in the light of its growing influence on the world stage. In any event, it is a development worthy of attention⁶.

Among business circles the concern has emerged that economic nationalism may be increasing in China and that, despite the progress in the process of reform and in particular in the legal framework, there may still be dangerous gaps in the legal certainty with which companies operate, which could even have an effect on the personal security of its employees.

This deterioration in the business environment is occurring in a context in which it is already considered that foreign enterprises in China face a large number of barriers. A study sponsored by the European Commission estimated that European exporters suffered a cost of 12,500 million Euros in 2004 as a result of lost export opportunities due to non-tariff barriers in China. Moreover, in three sectors of services (financial services, telecommunications and construction) it was estimated that the cost of lost business opportunities exceeded 8,900 million Euros. In total, therefore, a minimum of 21,000 million Euros was lost per year⁷.

Apart from some cases that have had a major impact and that we have mentioned in the preceding pages, a wide range of issues are the subject of complaints by foreign companies (and obviously European companies), such as government procurement, intellectual property rights, foreign investment restrictions, certifications, lack of transparency in law, arbitrariness in the decisions of administrative bodies, etc.

On these issues, which are reviewed in more detail in a later section of this paper, many companies have perceived a deterioration of conditions in the Chinese market, and making an assessment of this, and its appropriate correction, is an essential task in order to improve the perception of the business climate in the Chinese market among European companies.

The Chinese authorities have rejected accusations that there has been a change in China’s policy towards foreign investment. The Chinese Commerce Minister Chen Deming wrote in July 2010 (‘Thriving China is ever more open for business’, in the *Financial Times*) that ‘China has kept its market open through the financial crisis’. According to Chen, ‘in 2009, of 12,439 tenders for procurement of electromechanical products, 55% went to foreign investment enterprises’.

Regarding the issue of indigenous innovation, the Chinese minister pointed out that foreign companies established in China receive the same treatment as Chinese enterprises: 'all foreign enterprises are given equal treatment and [that] all their products are considered to be "made in China", while the same rules of origin are applied to them as to Chinese products'.

Chen recalled that in fact, despite these accusations, China remained a major destination for foreign investment: 'in 2009, global FDI dropped by nearly 40 per cent, but investment into China fell by only 2.6 per cent'.

Finally, Chen emphasized the beneficial role that, in times of crisis, the Chinese market represented for many international companies, citing the example of General Motors: 'in 2009, General Motors filed for bankruptcy in the US, but its sales in China grew by 67 per cent. It sold more than 1m vehicles in China in the first five months of this year, meeting half of its 2010 target of 2m ahead of schedule'⁸.

However, it should also be noted that in some business circles there is a significantly different view of this situation. We could summarize this view as the idea that problems do exist, there is nationalism and protectionism, but this must be considered as something irreversible and, nevertheless, China's market still offers good business opportunities. The key to success is to take advantage and be competitive, and to design an appropriate strategy.

This is the opinion of a major consultancy firm operating in the Chinese market, Interchina, that considers that the rise of protectionism is not a recent phenomenon. 'The early signs of increased protectionism date back to the beginning of this century'⁹.

According to Interchina, 'Probably the strongest hindrance to foreign participation in China's economy is the power wielded by Chinese companies, particularly State-Owned Enterprises (SOEs), and their government backers. These groups seek industry consolidation and limits on competition and are thus less willing to adopt good corporate governance practices including transparency and accountability'.

But the rise of protectionism and nationalism are compatible with the maintenance of business opportunities.

'Overall, though, the forces against protectionism have been fighting a losing battle and during the last decade China has completely changed its approach to foreign investment. That does not mean that there is no place for foreign investment in China, or that foreign companies are no longer doing well. It simply means that foreign companies need to learn to adapt to be able to create win-win opportunities (...) in spite of all the noise to the contrary, for most foreign companies business remains good. Foreign companies are enjoying the boom in China, with rapidly increasing sales volumes and in many cases considerable profits, as shown in surveys conducted by the European Chamber and the U.S. China Business Council'¹⁰.

Interchina managers Borgonjon and Hofmann take for granted that China will not open certain sectors to foreign companies: 'China is not renegeing on its commitments, but it also is not opening these sectors further. Many companies, in particular banks, mistakenly anticipated a further opening of the sector but this is not happening and is unlikely to happen within the next 10 years'¹¹.

In sectors where the level of protectionism is high, from wind power to cars, foreign firms can nevertheless conduct good business. 'Often the successful companies have long histories in China, and a thorough understanding of the market. They also have an experienced China team, with a strategy, which fits the development of its sector in China, and a competitive product offering'¹².

For foreign companies the key challenge is the capacity to be competitive, to understand and adapt to the market, to develop an appropriate relationship with the government.

'Being competitive in China requires a whole set of capabilities which are quite different from those required in developed markets. The key to such competitiveness is a strong local team, with strong decision making power and the freedom to work within a framework which is different than that used by the company in other markets, e.g. one which allows faster decision making, faster product development and/or different investment decision processes, etc. A sophisticated government relations approach which addresses the concerns of all stakeholders, not just the government, is essential'¹³.

Interchina arrives at the following conclusion about the business climate in China for foreign companies:

'Many issues affect a company's ability to run a profitable business in China today, and protectionism is but one. The majority of foreign companies are doing well, continue to see good opportunities in China's market and consider a whole range of issues in determining their market strategies. The main challenge for these companies is not protectionism, but the whole set of issues affecting their competitiveness in China. The market not only is booming, but it also is becoming more complex and sophisticated and competitors (mainly Chinese and Taiwanese) are quickly adapting to these changes. They are flexible, fast, have experienced local teams, understand the customer at all levels and all segments and know how to work with the government at different levels while controlling costs. Rather than focusing on market protection, foreign companies should focus their attention and their energies on the arduous task of becoming and remaining competitive in a very challenging market'¹⁴.

2.2. Irritants in bilateral trade

There have been irritants and disputes in EU–China bilateral trade for many years. However, in recent times we have seen an intensification of these conflicts.

We shall review in this section some of the major irritants.

2.2.1. The EU trade deficit with China

Underpinning this issue lies the strong growth of Chinese exports to European countries, much higher than the exports of the European countries to China, and the consequent increase in the trade deficit for the EU.

The causes of the sharp increase of Chinese exports and lower export growth in Europe are varied and cannot be attributed mainly to protectionism by China.

Overall Chinese tariffs are not high. However, it should be borne in mind that the average levels hide the existence of peaks in certain products and sectors, where tariffs can reach very high levels. This is the case of meat, with maximum levels of between 15 and 25%; certain dairy products, about 25%; 65% for wheat and rice; 40% for certain items of corn; 50% for sugar; up to 65% for drinks and tobacco; 50% for fertilizers; 20% for tyres; 38% for wool; 40% for cotton; between 15 and 25% for certain textiles and footwear; 25% in ceramic tiles; 35% for certain jewellery products; up to 35% for consumer electronics; 28% for cars; and 45% for motorcycles¹⁵.

In 2009, however, the EU trade deficit with China declined as a result of the negative impact that the economic crisis had on imports of European countries.

European imports of Chinese goods fell by 13% from 247,900 million in 2008 to 214,700 million in 2009.

It should be noted, however, that among the ten largest EU trade partners, China was the country with a smallest reduction of EU imports after Switzerland. EU imports from Brazil, for example, were reduced by 29%, from Russia by 35% and from India by 14%.

European exports to China registered a positive performance in 2009. China was the only country among the top ten trading partners of the EU that registered a growth of exports (4%). In all other cases, European exports fell in 2009 (by 18% in the case of Brazil, 13% in the case of India). The dynamism of European exports to China has to be necessarily associated with the strong economic growth that this country has maintained in 2009, despite the international economic crisis.

Thanks to these developments, the EU trade deficit with China declined by 21%, from 169,500 to 133,100 million Euros. This trend was quickly reversed, as China and the EU recovered the economic impulse. In 2010 European exports to China amounted to 113 billion, whereas imports from China increased by 31%, to reach 282 billion. This resulted in a trade deficit of 168 billion Euros, just below the 2008 record of 169 billion.

Moreover, the trade deficit of the EU with China must be subject to some qualifications in order that a fair assessment may be made of it.

First, the increasing trade deficit with China in recent times has been accompanied by a reduction of the trade deficit with other countries.

'During the (...) period 2000–2006, the EU's trade deficit with China rose from 49 to 130 billion Euros. But this is only half of the story. The other half is the *decrease* of the EU's trade deficit with the rest of the world – from 93 to 66 billion Euros. In short, this period has witnessed a massive reshuffling of global trade flows. Many trading partners of the EU

export to the EU via China – rather than from their home countries. This is particularly the case of nine large trading partners of the EU (Japan, Korea, Hong Kong, Indonesia, Malaysia, Singapore, Taiwan, Thailand, and the US)¹⁶.

As noted in a major study of EU–China relations:

‘Asia’s overall share of EU imports has risen only a little over the last ten years (by 10 per cent, according to the Commission). The reason is that many Chinese exports have replaced goods that previously came from countries such as Japan, Korea and Taiwan. These countries now ship components to China, where they are assembled and then sold as finished goods to world markets. Indeed, many European (and American) companies have their products put together in China. In 2005 such “processing trade” accounted for more than half of China’s exports (and about half the goods exported from China are from foreign owned factories). This shift of manufacturing from other Asian countries to China helps to explain why the EU’s overall trade deficit in medium technology goods did not rise much between 1999 and 2006, despite China’s spectacular export growth in such sectors’¹⁷.

Secondly, the strong growth of Chinese exports has been due to a large extent to the fact that its products are competitive and attractive. In this sense, European consumers have benefited from the expansion of imports of Chinese products, which have also contributed to the moderation of prices. According to one study, the availability of cheaper Chinese products has allowed European households to save an average of 300 Euros per year¹⁸.

Third, we must not forget that a substantial portion of the Chinese goods exported are manufactured by foreign companies installed in China, including European companies. Protectionist measures affecting China’s exports have thus a direct negative impact on many European companies.

In any case, despite the improvement registered in 2009, the trade deficit is a strong potential source of conflict, especially if the economic slowdown in the EU continues and the perception that Chinese products benefit from an unfair advantage is reinforced, as probably would happen if the exchange rate of the Chinese currency is considered to be at an artificially undervalued level.

‘China’s trade surplus with Europe will become an increasing source of friction. Unlike the Americans, the Europeans are not dependent on Chinese capital to help fund their fiscal deficits. As a result, they can afford to allow relations with China to deteriorate. So far, they have been very cautious about criticising China for fear of damaging their business interests in the country. But against a backdrop of very weak economic growth in Europe, high unemployment and a widespread perception that European firms are not being treated fairly in China, trade relations with Europe could easily worsen. The steep rise in the value of the Euro against the Chinese currency is a source of mounting anger in Europe, reflecting as it does China’s refusal to allow a meaningful appreciation of the RMB against the weakening dollar to which the Chinese currency is effectively tied’¹⁹.

2.2.2. EU protectionist measures against Chinese products

Adoption of protectionist measures against Chinese products has been recurrent in the European Union. The alleged unfair competition from Chinese products has been the argument most commonly used to justify these measures. Sometimes, scandals about the safety of Chinese products (potentially toxic toys, contaminated toothpaste) have helped to create a favourable environment for protectionist measures. Of the 1,600 notifications of unsafe products that the Commission received in 2007, half of them were for Chinese goods.

Chinese goods head the list of dangerous consumer products notified through the EU’s rapid alert system (Rapex) in 2009, according to a European Commission report published on 15 April 2010. China accounted for 60% of the 1993 notification cases during the year, with toys, clothing, textiles and motor vehicles turning out to be the chief culprits. Harm from dangerous chemicals, general injuries, choking, electric shocks and strangulation were some of the main problems cited by complainants.

Many of these European protectionist measures have been articulated through antidumping procedures, the most common barrier in the EU against imports of products from developing countries. Through these procedures some labour-intensive sectors (such as shoes and clothing), or sectors that have powerful lobbies, have tried to curb Chinese exports to European markets. In June 2011 the EU had 55 anti-dumping measures and one anti-subsidy measure in force against imports from China.

The number of antidumping measures against Chinese exports doubled between 1995 and 2008, while the total number of these measures imposed in the world grew by 16%. In this way, China has gone from receiving one fifth of antidumping measures in 1995 to receive more than one third in 2008. The sectors most affected have been footwear, transport equipment, especially bicycles, building materials and ceramic products, vegetable products, such as garlic, chemicals and steel²⁰.

Since 2002 the EU also began to adopt safeguard measures, beginning with a safeguard regarding the steel sector (which affected other countries besides China). In 2005 it adopted a new safeguard measure against a wide range of textiles and clothing products. Subsequent negotiations led to voluntary export restraints by China, capping the growth of exports in 10 of the 35 categories of textiles and clothing.

The effectiveness of these measures is disputed. As noted above, a large part of Chinese exports corresponds to foreign companies, including European ones, that ones that can be negatively affected by the adoption of protective measures for European markets.

‘Trade defence measures are based on an increasingly obsolete view of what a modern industrial economy is, namely a complex production process fragmented among a notable number of countries. Trade defence measures equate industry to manufacturing alone, ignoring the crucial *pre*-manufacturing step (design and preparation of the physical manufacturing processes) and *post*-manufacturing step (logistics, marketing, advertising, etc). These two steps generate a lot of value added in the importing country. For instance, even in labour-intensive products such as shoes, these two steps represent half to three quarters of the European value added in the shoe sector. In short, not only do antidumping and safeguard measures *not* protect the ‘old’ economy (the manufacturing step *per se*), but they might also hurt the ‘new’ economy (pre- and post-manufacturing steps)’²¹.

In February 2010, China filed a formal protest at the WTO against the EU tariffs on imports of Chinese shoes. In December 2009 the EU effectively agreed to extend for 15 months (from January 2010) anti-dumping measures against shoes from China and Vietnam, originally adopted in 2006. These fees add between 9.7 and 16.5% to the price of the shoes imported from China.

The extension of the antidumping duties revealed the existence of significant divisions among European countries. 13 countries voted against the extension, nine in favour and five abstained. According to EU rules on antidumping, abstentions are counted in favour of the proposal from the Commission.

The European Footwear Alliance, which represents several large European manufacturers (such as Adidas and Timberland) supported the Chinese decision to go to the WTO, saying in a statement that ‘[i]ronically, the measure hurts European business and consumers the most’.

In March 2010 the Federation of European Sporting Goods Industry (FESI), which includes companies such as Adidas, Puma, Nike and Lacoste, announced that it had decided to take legal action against the decision of the EU to extend antidumping duties on footwear. ‘We have taken this case to court not only because we firmly believe that these duties are unjustified but also because it is clear to us that the European Commission is ignoring the basic economic realities of the footwear business,’ FESI president Horst Widmann said in a statement²².

Presumably the implementation of such measures will continue in the coming years, especially considering that there are not good prospects for the EU to agree to China’s Market Economy Status (MES). China and the EU have conducted negotiations in relation to the MES, but there is a wide gap between the positions of the two parties. According to its 2001 protocol of accession to the WTO, China will definitively be awarded MES in 2016. Henceforth the adoption of protectionist measures against their products will become substantially more difficult. But until then, trade disputes, in particular the imposition of antidumping measures against Chinese products, will remain a potentially destabilizing irritant in trade relations.

2.2.3. The issue of the exchange rate of the Chinese currency

The exchange rate of the Chinese currency has become a major irritant in recent months. The alleged undervaluation of the RMB has led to growing discontent in the first place in the United States but also in Europe, and threatens to trigger a serious conflict in the near future.

The basic positions on the subject are well known. Relevant business and academic circles of Western countries believe that China is maintaining the exchange rate of its currency artificially low, in what amounts to a subsidy to its exports and increased tariffs on its imports. The competitiveness thus provided to exports is probably the key factor that has allowed the strong growth in exports and in the surpluses of the Chinese balance of trade, making China the country of the world with the largest amount of foreign exchange reserves (more than two trillion dollars at the end of 2009).

The assessment of the magnitude of the undervaluation of the RMB varies. According to one recent estimate of the undervaluation of the Chinese currency based on the purchasing power parity (PPP) approach, Arvind Subramanian, of the Peterson Institute for International Economics, finds that the renminbi is undervalued by approximately 30%²³.

In practice, China has kept the exchange rate of its currency tied to the dollar. In 2005 the Chinese government announced that the RMB's exchange rate would be tied to a basket of currencies, although the mechanism was not defined and it appears that the dollar has remained the central reference element.

This exchange rate policy has strongly affected European exporters. Between 2002 and 2007 the dollar fell by around 40% against the Euro, taking with it the RMB and other Asian currencies. This has produced a strong appreciation of the Euro against the RMB, with the consequent reduction in competitiveness of European exports.

One of the best known critics of China's exchange rate policy has been the economist Paul Krugman, who has strongly defended the need for the United States to take vigorous action:

'China's policy of keeping its currency, the renminbi, undervalued has become a significant drag on global economic recovery? (...) Today, China is adding more than \$30 billion a month to its \$2.4 trillion hoard of reserves. The International Monetary Fund expects China to have a 2010 current surplus of more than \$450 billion 10 times the 2003 figure. This is the most distortionary exchange rate policy any major nation has ever followed'²⁴.

The Chinese stance, as is well known, is first to defend that the exchange rate of its currency is a 'domestic' matter, that China has the right to manage independently, without negotiating with international partners. Secondly, China does not offer concrete indications of what its policy in this area will be, normally only giving very general statements in relation thereto: 'We will maintain the stability of the renminbi at a reasonable and balanced level', said Premier Wen Jiabao after the EU-China summit last December 2009.

In June 2010, shortly before a meeting of G20, the Chinese government announced that the renminbi's fixed peg to the dollar would be replaced by a more flexible system. The Chinese currency appreciated slightly in the following weeks. However, most observers and analysts rule out a major appreciation. Forecasts point rather to a slow process of appreciation.

It is important to remember that the situation of the Euro against the RMB is very different from that of the Dollar. In early 2010, largely as a result of the fall of the Euro caused by the problems of sovereign debt, the Euro depreciated sharply against the RMB, a process which must surely have a relationship with the improvement of trade balance between the EU and China.

2.3. Changes in the Chinese economic model of growth

There is a fairly general consensus among analysts of the Chinese economy that it needs to undertake a thorough rebalancing if it wants to maintain balanced and sustained growth in the long term. This rebalancing of the economy has broad implications on China and the international economy, and in regard to the subject of this paper, opens up new business prospects for European companies.

As noted repeatedly, Chinese economic growth has been based on investment and exports. China has spent more than 40% of its GDP on investment. According to the Asian Development Outlook 2010, in 2009 'total investment contributed 8 percentage points, or a record 92%, of total GDP growth on the demand side. The investment-to-GDP ratio rose to nearly 46%, the highest level in at least three decades'²⁵.

Industrial production accounts for nearly 50% of GDP, while services do not reach 40%. The saving rate of households is very high, while household consumption accounts for 35% of GDP, a very low participation in relation to most countries.

'Growth in consumption is limited by household income's declining share of total income. The share of household income in total national disposable income shrank from about 66% in 1997 to 58% in 2007, while the share of government income increased from about 17% to 20% and that of enterprises from 17% to 22%'²⁶.

According to Simon Tilford, 'At least in terms of the relative importance of industry and services, China continues to look much more like a communist country than a capitalist one'²⁷.

This structure of the Chinese economy has an important bearing on some of the issues that cause friction in the international community. China has produced much more than it has consumed, and the gap has been channelled to exports, largely, it is alleged, thanks to an undervalued exchange rate. Thus China has obtained such high trade surpluses with many countries which are a source of discontent.

China has also obtained a large surplus in its current account, which has allowed it to transfer a substantial amount of capital abroad, for example through the purchase of US treasury bonds.

There is general agreement that the new model of growth of the Chinese economy should be oriented according to the following trends:

- An increased share of consumption at the expense of savings and investment.
- Reduced weight of exports, which must be offset by increased domestic demand.
- A growth of services at the expense of industrial production.

To promote these changes, and in particular to encourage greater consumption and lower savings, it is necessary to further develop basic social services, especially education and health. If the propensity to save is so high, this is due largely to a matter of safeguarding against risks. Chinese citizens have to save in order to be prepared for medical expenses (which can be very high). They also have to save to finance the education of their children. As noted by Tilford,

'much has been made of the allegedly strong cultural disposition to save on the part of the Chinese. The Chinese may well be more cautious than the famously optimistic Americans. But the principal reason for China's high savings rates has little to do with culture and a lot to do with public policy. The absence of any meaningful social security system and the high cost of healthcare and other essential services relative to average incomes ensure that the Chinese have no option but to save a very high proportion of their incomes'²⁸

The Chinese authorities have for a long time indicated the desirability of encouraging this rebalancing in the growth model. The crisis, however, has slowed the change. The huge stimulus package launched by the Chinese authorities to counter the effects of the economic crisis has been implemented to a significant extent through an increase in loans to state enterprises, with which they have financed investments in infrastructure projects. To a lesser extent the stimulus package was aimed at boosting consumption. Thus the share of investment in GDP has even increased in 2009, as we mentioned earlier.

However, some authors have stressed that the negative effects on consumption of China's policy to tackle the crisis have been exaggerated. Nicholas R. Lardy, a foremost international specialist on Chinese economy, has written:

'The charge that the stimulus program focused excessively on expanding investment demand and has set back China's efforts to achieve more balanced growth by encouraging private consumption seems wrong. Consumption growth in 2009 was actually quite robust; indeed on the basis of preliminary data it appears that 2009 was the first year since 2000 that the growth of consumption outstripped the growth of GDP. Thus the long-term decline in the consumption share of GDP probably ended, at least temporarily, in 2009'²⁹.

According to Lardy, consumption has benefited from several factors:

- Increased investment, particularly in the construction sector, has offset much of the job losses in export sectors;
- The government has continued to increase transfers to lower income citizens, as well as pensions;
- The government has taken other measures to promote consumption, such as tax cuts for the purchase of cars, subsidies for the purchase of appliances by residents of rural areas, etc.;
- And finally, there has been a substantial increase in household debt, part of which went to finance the purchase of houses, and a substantial part to finance consumption expenditures.

‘Contrary to repeated criticisms, this stimulus had a substantial consumption component and directed investment primarily toward infrastructure rather than expanding capacity in traditional industries such as steel’, according to Lardy³⁰.

State spending on education and health has grown strongly in recent years but still has a long road ahead.

On the other hand, the structure of taxation should also change, with a reduced load on consumption and an increased load on companies. Increased corporate tax will reduce corporate profits and therefore investment. A lower tax burden on individuals will increase disposable income and consumption.

Similarly, the financial system should also be reformed in order to redirect funding from businesses to consumers. Interest rates on loans to state enterprises are very low, which encourages a high level of investment. For their part, consumer credit and mortgage credit are very underdeveloped.

The development of services also requires drastic changes. According to the Asian Development Bank, ‘unlocking the sector’s potential requires policy action on a long list of constraints’. The bank mentions in this respect:

- Excessive market concentration and entry barriers.

‘As a result, state-owned enterprises dominate services, a fact that restrains competitiveness and obstructs the entry of new players, thus reducing the benefits that greater competition and liberalization would bring. Entry barriers include administrative hurdles; opaque regulations; cumbersome licensing requirements; and restrictions on the geographic range in which businesses can operate, their legal structure, and their access to banking services’.

- Restrictions on direct foreign participation. ‘With the exception of a few subsectors, such as hotels and some types of banking, services remain largely closed to foreign firms’.
- Incentive bias toward manufacturing. ‘Fiscal incentives direct investment to the production of goods, and exemptions and rebates favor export of goods, discouraging investment in services’.
- Inefficient allocation of capital. ‘Large state-owned enterprises, including those in services, receive about two-thirds of total lending. In contrast, private enterprises get only one quarter of the credit available and face much higher interest rates’.
- Incomplete urbanization and labour market rigidities. ‘Service providers generally thrive in cities, where demand is strong and customers are concentrated in a relatively small area. While there are many cities, about 65% of the population still lives in far-flung rural areas. Urbanization has been slowed by rigidities in the labour market, in particular by the *hukou* system’.
- Underinvestment in education and training. ‘The policy investment bias favours the acquisition of equipment and materials, to the detriment of investment in training’³¹.

Finally, the exchange rate should play a key role here also. As indicated, the undervalued exchange rate is an export subsidy and favours in this regard firms (and investment), harming consumers. The appreciation of the Chinese currency would raise the income level of consumers and reduce the external competitiveness of Chinese products. This would encourage a reorientation of the bases of growth from exports to consumption.

Progress toward an exchange rate more in line with market forces would not only help to reduce conflicts with trading partners, but also favour the reorientation of the growth model that the Chinese authorities themselves have acknowledged as necessary.

In short, this process of rebalancing the Chinese economy, which seems both desirable and irreversible, has a broad impact not only on China but on the international economy. No doubt it will create, in certain aspects, challenges and difficulties for European companies. But it could also open up new niches of opportunity, as we shall discuss later.

3. Access barriers to the Chinese market

Despite the strong growth of trade and investment, there have traditionally been complaints about the problems of access to the Chinese market, by international companies in general and European companies in particular.

Early in the last decade the situation began to improve gradually, largely as a result of the commitments made by China with the access to the World Trade Organization. In the last two or three years, however, this trend seems to no longer apply. Entry barriers have increased dramatically, according to the general opinion of many operators, chambers of commerce, etc.

In its opening statement to the Trade Policy Review (TPR) meeting in Geneva on 31 May, the EU summarized its main concerns:

- The continued problem of non-tariff barriers in China. EU pointed to the burdensome regulatory regime, which is characterised by low alignment to international standards, the recurrent use of export barriers, and investment restrictions to foreign companies. For the EU it is also essential that China's innovation policy ensures open and fair competition without restrictions in terms of market access.
- The EU acknowledged improvements in Intellectual Property Rights protection in China, but emphasised the urgent need for greater enforcement efforts, including effective customs controls and criminal prosecution.
- The unjustified state interference in the economy persists. This is true notably in the manufacturing sectors, in which China has become a leader worldwide, such as automobiles. The Chinese government's guidance in allocating resources and official trade finance support are other examples.
- The need for greater transparency in policy-making and regular public consultations with foreign and domestic stakeholders. EU urged China to make its trade regime significantly more predictable and transparent³².
- The following is a brief overview of the main problems of access to the Chinese market.

3.1. Public procurement

European companies feel discriminated in public procurement. According to the European Chamber of Commerce in China, '[e]qual treatment for domestic and foreign companies is conspicuously absent in the public procurement process, and China's signing up to the WTO's Government Procurement Agreement (GPA) seems to be further delayed by a disappointing first offer from the Chinese side'³³.

The European Chamber of Commerce mentions for example licenses for wind farms, 'a sector in which not a single foreign wind turbine manufacturer has won a bid since 2005'³⁴.

When China joined the WTO, it agreed to start negotiations as soon as possible to become a signatory to the Agreement on Public Procurement. China currently has observer status.

'The Chinese proposal on the coverage of its offer can be described as disappointing. Among other shortcomings, it does not include sub-central entities (representing 80% of the total Chinese procurement), public enterprises and services sectors of most interest to European companies (transport, electricity, telecommunications, construction, infrastructure and public works etc.). It also establishes thresholds too high, so that large number of tenders would not be subject to the provisions of the agreement. Similarly, the transition period of 15 years since its membership is clearly excessive'³⁵.

Beijing presented a second proposal to the GPA (Government Procurement Agreement) – which includes the

US, Japan and all 27 European Union member states – in July 2010. It seems unlikely that this new proposal can be accepted, as it does not include substantial progress from the previous proposal. In an analysis of the Chinese proposal, the *Financial Times* indicated that the new text retained the key limitations of the previous one:

‘[T]he main concern about China’s latest proposal is that it does not offer foreign companies access to local government and state-owned enterprise procurement contracts, which account for the vast majority of state contracts in China. Another stumbling block is China’s proposal to only open government construction contracts to foreign companies if those projects are larger than a threshold three times higher than most other major GPA members’³⁶.

Noteworthy in the area of public procurement is the entry into force in late 2009 of new rules on promoting domestic innovation (‘indigenous innovation’), which have aroused serious concerns among foreign companies.

With these rules the Chinese authorities try to promote the development of technologies owned and developed by Chinese companies, and reduce reliance on the use of foreign technologies. Indigenous innovation products will enjoy preference in public procurement.

To qualify as an indigenous innovation, a product must

- Have been produced by an enterprise that has full ownership of intellectual property rights in China either via its own technological innovation activities or because the Chinese enterprise, work unit, or citizen has, by legal means, obtained the Chinese rights;
- Have a trademark that is owned by a Chinese company and registered in China;
- Embody a high degree of creativity and innovation;
- Offer a strong degree of reliability and dependable quality, with certification from the China National Certification Administration or its provincial departmental branches.

There are six areas identified for inclusion in the indigenous innovation catalogue: computer and application devices, communication products, modern office equipment, software, new energy equipment and energy efficient products.

‘Over the past three years, a few provincial and municipal governments have developed their own product catalogues, which include lists of products accredited as indigenous innovation. To date, very few products made at a foreign-invested facility have received accreditation. Of the 523 products listed in the Shanghai catalogue, only two are made by foreign-invested enterprises (FIEs) and those are from Chinese-foreign joint ventures with majority Chinese ownership. Of Beijing’s 42 qualified products, just one comes from a foreign company’³⁷.

Foreign companies established in China fear that it will be very difficult to obtain the accreditation of local technology.

‘The biggest obstacle for foreign companies is the requirement that the applying China entity fully owns the IP and first register the trademark in China. The primary concern of foreign companies is that they will be excluded from China’s government procurement market simply because they have developed IP and owned trademarks in other jurisdictions’³⁸.

In reality, the situation, as in so many other issues, is not clear. Probably as a response to the criticism of foreign companies, the Ministry of Science and Technology published a document in April 2010 that said that any company whose products conformed to Chinese laws, regulations and technology policy and which possessed legal rights to the related intellectual property could gain accreditation under rules on ‘indigenous innovation’ to bid for government contracts.

The American Chamber of Commerce published in March 2010 the results of a survey of U.S. companies in connection with the new innovation policy, which reflected the concern and pessimism about the impact of new regulations.

‘Although the current policy only targets select industries and has not yet been implemented, 28 percent of American companies responded that they are already losing out on business as a result of indigenous innovation (...) Looking more closely at the *Innovation Policy Survey* data, among American high-tech companies (whose industries have been targeted), 57 percent report that they expect to lose business because of indigenous innovation policies. Overall,

more than 40 percent of companies responded that they expect to be negatively affected by these policies once they are fully implemented³⁹.

According to some analyses, the new rules on indigenous innovation are the expression of a more general, and worrying, shift in the politics of China in its foreign economic relations. According to a 2010 publication of the U.S. Chamber of Commerce,

‘...while indigenous innovation is considered by China to be a bold second act of Deng’s reform and opening, in the West the campaign is increasingly perceived as anti-foreign and regressive. Indigenous innovation seems to be a policy borne as much out of China’s fear of foreign domination as China’s pride in its great accomplishments and desire to be a leader in the rules-based international system. For many multinationals – especially tech companies – the policies appear to signal that the pretence of goodwill is gone. The belief by foreign companies that large financial investments, the sharing of expertise and significant technology transfers would lead to an ever opening China market is being replaced by boardroom banter that win-win in China means China wins twice (...) The indigenous innovation campaign and surrounding web of industrial policies represent the beginning of a new era in not only the US-China economic and political relationship but in China’s relationship with international business and the developed world⁴⁰.

3.2. Restrictions on foreign investment

The activities of foreign firms in the Chinese market are severely constrained by existing legal limitations on foreign equity participation in many sectors.

Some examples of these limitations, which especially affect European companies, are:

- **Cars.** There is still a rule requiring the establishment of 50/50 joint ventures. As noted by the European Chamber of Commerce,

‘[i]t is remarkable that, at a time when Chinese investors are acquiring numerous European auto makers, Europe’s own car makers can still not establish their own car manufacturing facilities in China. Incredibly, market access conditions for these auto companies have hardly changed in the three decades since the reform and opening up policy began. To operate in China, they are still forced to establish 50/50 joint ventures just as they were 30 years ago⁴¹.

The lack of reciprocity may be particularly striking in the case of automobiles. As noted in an article by the president of the European Chamber of Commerce in China, foreign firms ‘are asking why Geely can buy Volvo, while foreign motor manufacturers still have to form joint ventures to manufacture their cars in China’⁴².

- **Clean Development Mechanism.** Chinese law requires joint ventures with 51% of Chinese capital in the projects under the Clean Development Mechanism. ‘As a consequence, not one of the world’s top five wind operators has a single wind development project in China’⁴³.
- **Computer Reservation Systems.** Foreign firms are unable to provide services directly to travel agents and airlines in China. This particularly affects Amadeus, the reservation system based in Madrid.
- **Banking.** The ceiling on foreign investment per company is 20% for the individual shareholder, and 25% for total foreign holdings.

Chinese law includes significant restrictions on foreign capital participation.

The ‘Guidelines for state-owned enterprise reform’, approved on December 2006, gave a list of sectors in which the state should be the sole owner or have a majority share. Among the sectors covered by these restrictions are power generation and distribution, oil, petrochemicals, natural gas, telecommunications and armaments. Moreover, the state must have a controlling stake in the coal, aviation and shipping industries.

In December 2007 a new ‘Catalogue for the guidance of foreign investment industries’ was published. The catalogue classifies industries for potential investment as prohibited or restricted (for instance, only permitted in a joint venture with a Chinese partner) or encouraged (investments the government is willing to support). The investments that do not fall into one of the three categories are considered permissible, but they are not entitled to receive policy incentives.

'New industries on the list of encouraged FDI are, for instance, modern agricultural methods, resource conservation and environmental protection (e.g. recycling, renewable energy, clean production), services outsourcing and modern logistics, advanced or new technologies and new materials. On the other hand, FDI in certain kinds of basic manufacturing that China has clearly mastered (e.g. clothing) will be permitted, but no longer encouraged. Foreign investments in highly energy- or resource-intensive and highly polluting projects are now either restricted or have been added to the prohibited category, which also includes mainly strategic and sensitive industries such as mining of certain minerals (e.g. tungsten, rare earths). The restricted category includes, for instance, the smelting of various metals, telecommunication companies, printing of publications and the construction and operation of high-grade real estate'⁴⁴.

At this point the relationship between greater openness to foreign investment in services and the necessary orientation of China towards a new model of economic growth must be taken into account. Foreign investment, particularly European investment, has great potential to stimulate the development of services that support the expansion of consumption, which in turn would encourage imports, reducing trade surpluses and so favouring a more balanced exchange rate of the Chinese currency.

Foreign direct investment in services contrasts in this regard with the investment in manufacturing sectors, which stimulates the production of goods for export with its consequent impact on trade disputes.

3.3. Certifications

In certain sectors requirements for certification to operate in the Chinese market are being introduced, certifications that may be difficult to obtain for foreign companies.

The European Chamber of Commerce in China gives an example of such problems:

'A successful Chinese Wholly Foreign Owned Enterprise (WFOE) has for many years used commercial encryption technology to provide solutions for Chinese banking, telecoms and public transportation companies – the great majority of which are state-owned. However, this Company is finding it increasingly difficult to do business in China, because its clients now require product certifications from the Office of Security Commercial Code Administration (OSCCA). Whilst relevant regulations do not exclude foreign or foreign-owned companies from OSCCA certification, no such companies have been certified to date. Additionally, the OSCCA certification is a precondition for the China Compulsory Certification (CCC) certification which will be required for commercial encryption products purchased by any Chinese government agency from May 1st, 2010. Based on experience, there is a serious risk that, in practice, the company's state-owned clients will also start procuring only those products bearing the CCC mark'⁴⁵.

Another sector hit by regulatory protectionism is that of mobile phones. China approved new emission standards that require expensive and complicated testing of foreign models that had already passed EU and other international testing. 'Most of these tests are simply revenue-earners for the ministries that charge for the certificates,' according to Duncan Clark, the chairman of BDA, a technology consultancy in Beijing, 'and they appear designed to make life hard for foreign manufacturers.'⁴⁶

3.4. Lack of transparency in regulations

The lack of transparency in the rulemaking process, discretion in implementation of rules and a lack of coordination between government bodies, are factors that can negatively affect the activity of foreign companies.

One can again turn to the European Chamber of Commerce for the description of a particular and famous case, the blocked acquisition of Huiyuan Juice Group Ltd. by Coca-Cola, under Article 28 of China's Anti-Monopoly Law (AML).

'This was the first time MOFCOM blocked a merger after the AML came into effect on August 1st, 2008. A brief statement outlining MOFCOM's decision in this case was published on the Ministry's website. However, although the statement outlined the primary areas of concern in relation to the transaction, it offered very little detail about the case and, in particular, contained no substantive analysis or evidence supporting the decision to block the deal. Nor did it include any information on key issues such as the market definition or the balancing of the positive and negative impacts of the proposed deal on industry competitiveness. The lack of detail about the decision was widely criticized, and a MOFCOM spokesperson subsequently gave a media interview in which further information about the Ministry's investigation and conclusions were provided'⁴⁷.

3.5. Arbitrariness in the operation of the government

In recent years complaints about arbitrary conduct of the Chinese government have intensified.

‘China’s move towards economic openness has slowed noticeably since 2006, and there have been various setbacks and reversals. Nontariff barriers to trade make it hard for foreign exporters and investors to do business in China. These include unclear or arbitrary health and safety requirements; licensing and registration rules that discriminate against foreign companies; subsidies for Chinese companies through direct cash payments, cheap energy or soft loans; public tenders that are opaque and inaccessible for foreign bidders; and the widespread violation of intellectual property rights (IPR). Trade commissioner Peter Mandelson claims that non-tariff barriers and discriminatory rules cost European companies 55usd million a day in lost business opportunities. The EU Chamber of Commerce in Beijing reports a long list of complaints from its member companies about China’s bureaucracy, which can be obstructive and un-transparent. Examples include the imposition of proprietary technical standards to replace Western ones; the sudden announcement of new laws on taxation or foreign investment, without prior consultation or sufficient time for implementation; and the use of ‘impossible’ regulatory requirements in sectors that are, in theory, open to foreigners’⁴⁸.

3.6. Intellectual property protection issues

The problems of intellectual property protection have long been cited as one of the most important problems faced by foreign companies in the Chinese market. The Chinese authorities have made important efforts to promote intellectual property protection, but this is not yet as effective as it should be.

In 2005 the EU and China established a working group to address these problems. On the other hand, the US launched WTO consultations proceedings against China for breaching the obligations to protect intellectual property, in which the EU has officially requested to participate as interested party.

Intellectual property rights remain a serious problem for many European companies. According to the European Commission,

‘...seven out of ten European companies operating in China say that they have been the victim of IPR violations. In 2007, European manufacturers estimated that the loss of intellectual property costs them 20% of their potential revenues in China. Rates of counterfeited European products were reported to be around 5–10% of EU companies’ turnover in China’⁴⁹.

The EU objective is to increase the pressure on the Chinese authorities on issues such as payment of royalties, audiovisual piracy and, in particular, the need to strengthen the pursuit of crime in this area.

3.7. Geographical Indications

The protection of Geographical Indications (GI) of origin is another area of concern for the European Union.

In the second session of the EU–China High Level Economic and Trade Dialogue, in 2009, it was agreed that the EU and China would launch formal negotiations on an agreement for GI.

4. Windows of opportunity

As seen in the preceding pages, there are significant barriers to trade and investment between China and the European Union. However, these obstacles should not be perceived in an exaggerated way: the trend of recent years has clearly been towards expansion of bilateral relations. Both parties should strive to overcome the problems that arise. Despite the difficulties of the Chinese market, thousands of companies around the world continue to come to it, which proves that is an attractive market and offers good business opportunities.

Trade and investment between Europe and China continues to offer many areas of opportunity. In this section we review some of the windows of opportunity we see as most significant:

4.1. Opportunities in consumer goods and services in the Chinese market

With economic growth and rising living standards in China, European companies have a wide range of opportunities in the consumer goods sectors in which Europe has a long experience and tradition, with numerous internationally renowned brands. As noted in preceding pages, the new model of growth of the Chinese economy has to move towards a greater weighting of consumption.

The key objective is the sector of China's population with a high income level, which is concentrated in urban areas. Professionals, business managers and senior officials, are purchasers of goods and services in which European companies already have a real market, but with a huge potential for future growth.

This high-income sector is a relatively small proportion of the population but represents, given the existing income inequalities in China, a high proportion of the national income. Some studies estimate that in 2004 10% of households accounted for 35% of total income, and that 20% of the more affluent households accounted for more than 50% of income. Other studies show that the affluent Chinese middle class may be about 300 million people.

To the extent that China moves towards a new economic model with an increased share of consumption and services, European companies will find business opportunities in diverse sectors such as health, tourism, education, food, trade, etc., provided that barriers do not hinder their activities.

4.2. Green technologies

A sector that must be given special attention is that of new energy and climate change, in which there is already a well developed relationship between the EU and China. Europe is already a significant investor in green technologies in China. European companies are investing substantial amounts in Chinese projects aimed at reducing greenhouse gas emissions under the Clean Development Mechanism of the Kyoto Protocol, while the EU spends 60 million Euros per year in official bilateral cooperation on issues of climate change. The European Investment Bank has a credit facility of 500 million Euros to invest in projects aimed at reducing carbon emissions in China.

European companies are very active in this field and account for 80% of the market for emission reduction credits under the Clean Development Mechanism, a market estimated globally at 20 billion Euros in the period 2008–2012.

The Chinese authorities have realized the importance and impact of climate change, but must seek a delicate balance between decarbonization and the impact on economic growth and employment. On the other hand, China sees correctly that the change towards low carbon levels is an opportunity to move up the value chain in the production process.

There have been various types of proposals to strengthen cooperation between the EU and China in these fields.

'The establishment of a senior EU–China low carbon economy taskforce has been proposed, with an agreed work-plan and mandate to produce joint initiatives over the coming year. In terms of flagship projects, one critical area where progress is required is on the EU–China CCS demonstration plant that was agreed at the 2005 EU China summit. The targeted completion date of 2020 for this project has been overtaken by events, with the EU itself planning to complete eight to ten CCS projects by 2015 and with at least eight other major CCS demonstration plants underway in the US, Australia, Norway and Canada. The summit could build on the extensive work carried out on this project to date by agreeing to complete the CCS plant by 2015, make it a full part of the knowledge sharing process under the EU's CCS demonstration programme, and agree to jointly identify a workable financing mechanism by May 2010. A credible aim would be to have completed the selection of a demonstration site and a commercial consortium in advance of the next EU China summit⁵⁰.

The climate change issue is of great relevance, in two ways. On the one hand, it offers opportunities for cooperation between European and Chinese companies and institutions. On the other hand, we must not forget that disagreements over how to tackle climate change globally have a dangerous potential for becoming a source of confrontation.

Many analysts believe one of the reasons for the failure of the Copenhagen summit in 2009 was China's refusal to accept quantitative commitments to reduce emissions.

'If the Chinese continue their current line of resisting quantitative targets for cutting CO2 emissions, the Europeans may feel they have little choice but to take punitive action. Many European industrialists, and some EU politicians, are already talking about the need to apply 'carbon tariffs' to goods from China or other countries that shun any post-Kyoto system for curbing carbon emissions. China sees such talk as de facto protectionism, driven by fear of its economic success'⁵¹.

The climate change issue can become a major source of conflict between the EU and China. Some Western countries have advocated the adoption of punitive measures against countries that do not take strong enough measures to address the threat of climate change, such as special tariffs on imports of such countries. The adoption of such tariffs would probably open the door to a wider trade war.

4.3. Cooperation in third markets

There is a broad field of cooperation, as yet little explored, among Chinese and European companies in third markets, for the joint development of projects in the industrial field, infrastructure, energy, etc.

The basis to establish business collaboration must be the existence of a synergy of contributions, whereby both parties perceive a benefit from the potential alliance.

In principle, there are four major factors of synergy on which to base partnerships between European and Chinese companies to carry out industrial and technological projects in third markets:

- 1 – Technology. There may be projects in which Chinese or European companies do not have the appropriate technology, and this could be provided by the other party.
- 2 – Financing. When the size of a project, and funding required for it, makes it difficult to offer it from a single country, there is an obvious basis for an alliance. The increasing availability of foreign exchange reserves has already made China a lender of increasing importance to developing countries.

Some European companies have already begun to consider or negotiate the use of Chinese financing for projects in other countries. This is one of the aspects that most clearly mark the changes that have occurred in the Chinese economy. From being a major recipient of funding in the past, China has become a potentially major external financing source, both through direct investments and loans. Given the increased willingness of China to lend to countries in which the ability to obtain funding from Europe may be limited (such as African or Latin American countries), the use of Chinese financing by European companies has considerable potential to become a major issue of bilateral cooperation.

Repsol's alliance with China's Sinopec in Brazil, to develop oil fields of the Spanish company in this country, is a significant example of this strategy of combining resources. Repsol needs funds to develop these fields, funds obtained through the incorporation of Sinopec.

- 3 – Prices. One of the two parties has very competitive prices in certain types of goods, machinery, services. There have been already a number of cases in which European companies have incorporated in their offers equipment manufactured by Chinese companies, more competitive on price. Chinese construction companies can also be very competitive partners for projects in areas such as Asia, the Middle East or Africa.
- 4 – Commercial Support. One of the two parties can have a commercial presence and market knowledge that the other party lacks.

The great challenge is to identify specific cooperation possibilities, where these complementary factors can be put into action. To this end, it is necessary to increase mutual knowledge among European and Chinese companies.

The celebration of 'partnership seminars', organized by business entities such as the chambers of commerce or business associations that several European countries have with China, could contribute to this mutual understanding and to the exploring of specific opportunities for cooperation.

4.4. Chinese investments in Europe

The issue of investment of Chinese enterprises in European countries is an issue that, on one hand, offers significant business opportunities but, on the other, presents difficulties and gives rise to misgivings of various kinds.

Investment by Chinese enterprises in Western countries has sometimes been viewed with suspicion. In some cases, significant investment operations have ended up being blocked in the destination countries. In 2005 a Chinese oil company, CNOOC, tried to buy a U.S. company, Unocal, but the operation failed due to opposition from Congress and the government of the United States. In late 2008, Chinalco, a Chinese state company in the aluminium industry, reached an agreement to increase its stake in Australian mining company Rio Tinto. The opposition from the shareholders of Rio Tinto and distrust on the part of the Australian authorities scuppered the transaction.

In both cases the state character of the Chinese buying companies was a key factor in the opposition to their investment. There are also misgivings relating to the delivery of control of strategic assets to companies controlled by a foreign government.

Fears have also been expressed over the fact that purchases by sovereign funds may involve the transfer of companies to governments that do not share the same principles politically and economically, something that can be applied to Chinese sovereign funds. According to Grant,

‘Many politicians and a growing number of voters in Europe and the US are nervous that such huge sums are being managed by funds linked to governments that are not unequivocal supporters of economic or political freedom. Even those who are relaxed about the potential political agendas of SWFs express concerns about the low standards of corporate governance and transparency of certain funds. Although some SWFs are managed professionally and at arm’s length from the state, others have close institutional and personal links with authoritarian regimes’⁵².

In this regard, in 2008 the European Commission issued a communication on sovereign wealth funds in which it called on Member States to keep open their economies, but at the same time demanding that SWFs have certain minimum requirements of transparency and accountability.

European officials, both at the level of member countries and from the Commission, should study and reflect on this issue, and establish lines of action. China has launched an ambitious ‘Go Abroad Policy’, encouraging Chinese companies to invest abroad, with the primary aim of ensuring raw material supplies, but also for other reasons such as market expansion, access to new technologies, etc.

A key basis for Chinese policy is the availability of substantial foreign exchange reserves. In 2007 China established a sovereign wealth fund, China Investment Corporation (CIC), which was provided with US \$ 200 billion, two thirds of which must be invested in China and one third abroad. CIC acquired a stake in investment bank Morgan Stanley and in the Blackstone investment fund.

5. Some recommendations

In this final section we are going to formulate some suggestions on strategies and measures that could be useful in encouraging commercial relations and business cooperation between the EU and China.

- Prioritizing issues

It might be appropriate to establish an agenda of priority issues, which would focus the efforts of dialogue and negotiation between the EU and China. Currently the EU and China have agreements and negotiations on many subjects. Defining priority areas and issues could contribute to further progress.

Some of the topics that could have this priority are:

- Clean energy and climate change, in which there is already considerable collaboration, as we saw, and great opportunities for the future.
- The restrictions in China on foreign investment.
- The public procurement policy, which is a third area of great importance and of grave concern to many European companies.

- Chinese financing for projects developed by EU companies, as well as Chinese investments in Europe.
- Dialogue on the exchange rate of the Chinese currency

The dialogue on this difficult and complex topic could contribute to a more balanced view of it. China must assume that the exchange rate of the currency is not an entirely domestic issue that can be managed with total autonomy. The exchange rate of one currency expresses its price in terms of other currencies.

- A careful and nuanced approach to trade irritants

Trade irritants should be studied and tackled with extreme care. On issues like the exchange rate of the Chinese currency, or the alleged dumping of Chinese products, the situation may be much more complicated than might at first appear, as we have had occasion to analyse in the preceding pages.

In regard to action by the EU, it is important to listen to and take into consideration the views of the various business sectors affected. We have seen examples of antidumping measures taken by the Commission which have been vigorously challenged by certain industrial sectors (as has happened with antidumping measures on footwear, which have been challenged by major European manufacturers).

The EU, in its trade disputes, should as far as possible seek multilateral channels in which to address them. The position of the EU will be stronger when embedded in a multilateral framework for each case than in a strictly bilateral context.

- Clarification of the business environment in China for foreign companies

We believe that it is important that China convey messages, backed up by specific measures that reduce the uncertainties that have arisen in recent times in the business community about the business climate in China.

As seen in the first part of this work, since 2009 there has been a sharp deterioration in the perception by international companies of the business framework in China. Some specific incidents (Google, Rio Tinto) have contributed heavily to propagating the idea that foreign firms are no longer as welcome as they used to be in the Chinese market. The Chinese authorities should seek to clarify this issue, affirming, as is expected to be the case, that China has not entered a period of nationalism and economic protectionism.

In any case, the Chinese authorities must explain as clearly as possible what their policy is, and what the business context is for which foreign companies should prepare. Companies need a clear definition of the business context they face. Uncertainties have a negative influence on business activity.

Thus, the Chinese authorities must identify what are the sectors in which they intend to maintain restrictions on foreign investment in the medium and long term, and what will be the policies that will favour domestic technologies in public procurement, to cite two of the hottest issues at the present time. European companies would then know what to expect, and could develop appropriate strategies in relation to the Chinese market.

European companies may also discuss these issues with senior officials of the EU and their national governments, and design a strategy for negotiating with China, both bilaterally and multilaterally. These issues could then be raised under the High Level Economic Dialogue between China Trade and the EU. They could also be raised in the course of negotiations for granting China Market Economy Status, a status that China would have great interest in obtaining from the EU.

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Chapter 9

Understanding China's Competition Law & Policy: Merger Control as a Case Study

Jerónimo Maillo

1. Introduction

On the first of August of 2008, the Chinese Antimonopoly Law (hereinafter AML) entered into force¹. Great expectations were created regarding the impact of the new provisions on business operations in China and international transactions of companies active in the Chinese market.

The AML set up, for the very first time, a comprehensive system of competition provisions including rules on cartels and restrictive agreements, abuses of dominant position, merger control, public measures distorting competition and the promotion of free movement and establishment within the Chinese market. The AML consolidated dispersed, under-implemented and unsatisfactory former rules but went far beyond, importing many tools and concepts from mature antitrust jurisdictions like the US or the EU.

However, there was a great uncertainty as to whether and how the AML was going to be implemented and applied. Concerns were raised on whether the new rules would facilitate the creation of a level playing field in China or would be used as another protectionist tool against foreign companies. More than three years have elapsed since the entry into force of these new rules and we now have sufficient data to make at least a preliminary assessment of their application, in particular in certain areas such as merger control.

Indeed this chapter exclusively focuses on merger control as a case study of China's Competition Law. This decision is based on the three following reasons:

- (1) Merger control has been the first area to have implementing regulations and guidelines;
- (2) Consequently, we can already count on more than three years of effective practice (August 2008–October 2011 is the period herein examined);
- (3) More than 200 cases have already been decided by the Chinese authorities and, even more important, 9 decisions have been published –8 conditional clearances and one prohibition decision– some of them involving controversial issues.

All this makes merger control the best field for our research.

This chapter is structured in two main sections. After the introduction, the first section reviews the design of China's merger control, mainly looking at the AML provisions and the implementing regulations and guidelines. This section covers jurisdictional issues such as the concept of concentration or the thresholds above which prior notification is compulsory, institutional aspects (which authorities are empowered to apply the AML and how they are designed), procedural issues (how and who should notify, procedural phases, sanctions in the event of non-compliance, etc) and the substantial test to prohibit or clear a concentration (including not only

the core test –‘actual or potential elimination or restriction of competition’– but also other connected issues such as the efficiency or the failing company defences, remedies and conditions, or the consideration of other non–competition concerns such as ‘national economic development’ or ‘national security’).

The second section reviews the three years practice from August 2008 until October 2011 and in particular the 8 conditional clearances and the prohibition decision in the Coca–Cola case. It is very interesting to see how the Chinese authorities have dealt with these 9 cases, which competition concerns have arisen and which remedies/conditions have been deemed sufficient to clear the acquisition or why the operation was prohibited. The analysis takes into account the Chinese context but looks into the reasoning and the conclusions reached by the Chinese authorities in the light of more mature competition systems, in particular the EU’s rules.

Finally, some conclusions and policy recommendations will be drawn.

2. The formal design of China’s merger control

2.1. An overview of key jurisdictional and procedural issues

The AML sets up an *ex ante* merger control applicable for the very first time to both domestic and foreign companies². The basic regulation is contained in Chapter IV (Articles 20–29) of the AML entitled ‘concentration of business operators’, and was afterwards developed through several implementing regulations and guidelines such as the Provisions on Thresholds for Notification of Concentrations of Undertakings (hereinafter the Notification Thresholds Rules)³ and the Measures for the Business Operator Concentration Examination (hereinafter the Concentration Review Rules)⁴ dealing with procedural and jurisdictional issues (information required, notification form, calculation of turnover or voluntary filings). More recently, Provisional Rules on the Implementation of Acquisitions or Divestiture of Assets or Businesses for Concentrations of Business Operators (hereinafter Provisional Divestiture Rules) and Provisional Rules for Assessing Competitive Effects of Concentration of Business Operators (hereinafter Provisional Merger Assessment Rules) have been issued⁵.

A compulsory pre–merger notification system for all concentrations above certain thresholds and a one–stop shop competition review of those concentrations was established. This means that, within China, there will be only one notification and procedure, one applicable law (the AML and its implementing regulations), one competent authority (Ministry of Commerce, hereinafter MOFCOM) and therefore only one single competition review of each concentration. However, this does not imply that the concentration could not be simultaneously subject to other reviews responding to different concerns such as, *inter alia*, the so called ‘foreign investment entry review’ and/or the ‘national security review’⁶. Voluntary notification of other concentrations or *ex officio* competition review of concentrations below the thresholds was also foreseen in exceptional cases.

A concentration was defined in Article 20 of the AML and includes:

- (1) the merger of business operators;
- (2) acquiring control over other business operators by virtue of acquiring their equities or assets;
- (3) or acquiring control over other business operators or the possibility of exercising decisive influence over other business operators by virtue of contract or any other means.

The concept of concentration is therefore drafted in similar terms to those enshrined in EU legislation, in particular in Article 3 of Regulation 139/2004 on the control of concentrations⁷. Although the EU provision is much more detailed, the essence of the concept seems to be the same: an acquisition of economic control over a business operator, by whatever means (either by an acquisition of equities, assets, contract or any other means, including therefore acquisitions of *de facto* control).

It is very significant in this regard that the definition of ‘control’ –the core of the concentration concept– is exactly the same in both regimes: control is ‘the possibility of exercising decisive influence on other business operators’⁸. In the EU, the concept has been thoroughly explained through detailed guidelines of the European Commission and practice⁹. In the Chinese system, implementing guidelines are still silent on this issue. Moreover, as practice is scarce and not very transparent, we will have to wait to see how the concept is interpreted and applied and therefore whether the common formal definition in both systems also results in a common interpretation in practice.

In spite of similarities, a comparison of the EU and Chinese provisions regarding the notion of concentration reveals an important difference: Article 20 AML does not explicitly require the ‘durable’ character of the change of control as the EU legislation does. Thus, a first uncertainty arises about whether Chinese authorities would require notifications of non-durable restructurings and changes of control. If we take into account the strong similarity between the Chinese and the EU legislations in most aspects related to the definition of concentration and the fact that the ‘durable character’ is a key aspect of the EU concept, the absence of this key aspect in the AML is particularly bizarre and may suggest that it was intentional and maybe aimed at opening a door to enlargement of merger control scope. All this has very important practical consequences and it could potentially lead to a large-scale extension of the mandatory notification system and therefore the prior control of certain acquisitions by the Chinese authorities. In case the Chinese authorities opt to extend the merger control to non-durable acquisitions, they would be creating a substantial difference between the EU and the Chinese merger control system and a strong divergence from best international practices. Only administrative practice and/or guidelines will likely solve this uncertainty; we hope this is so, considering that only durable changes of control should be subject to merger control.

Another uncertainty regarding the concentration concept in the Chinese system refers to whether minority acquisitions and joint ventures are deemed to be concentrations:

- With regard to joint ventures, EU legislation has always included certain joint ventures within the concept of concentration, although the categories of joint ventures falling under the EU merger control have changed over time¹⁰. Nowadays, the creation of a durable full-function joint venture is a concentration according to Article 3.3 of Regulation 139/2004. Moreover, where the joint venture is not created *ex novo* (e.g. the acquisition of a pre-existent undertaking) the full function character will not be required and the joint venture will also qualify as a concentration, under article 3.1, b) of Regulation 139/2004. In contrast, the AML is silent on this issue. Although modelled on the EU system, its merger control chapter does not include any reference to joint ventures. The implementing rules are also silent: although some old draft measures seemed to state that full-function greenfield joint ventures would be seen as concentrations, the final text of the implementing measures omitted any reference regarding joint ventures. In practice and at least up to now, MOFCOM seems to take the view that joint ventures (regardless of whether they are full-function or not) should be notified and subject to merger control¹¹. This is consistent with pre-AML practice under the M&A guidelines for foreign mergers, but not with other international merger control practices such as the EU and USA systems¹². The Chinese system seems to be developing a more expansive concept of concentration and therefore more extensive notification duties.
- With regard to minority acquisitions, all we know is that, according to Article 20 AML, all acquisitions of shareholdings not conferring control (that is to say, decisive influence) are not deemed to be concentrations. However as neither the AML nor the implementing guidelines provide further explanations of this concept, many uncertainties still remain. Previous draft guidelines laid down that control was obtained when the acquirer gained the ability to decide certain strategic decisions (appointment of management, budget, operations and sales, substantial investment and other management and operational strategies), but this guidance was removed from the final text. Until more detailed guidelines are issued, it is better to be cautious and clear up possible doubts through pre-notification meetings with the Chinese authorities. Up to now, practice suggests that the acquisition of a veto over certain strategic decisions could suffice to acquire control, just like in the EU.

Intra-group restructurings are exempted from mandatory notification under both regimes although the regulation is not exactly the same. Article 3 of Regulation 139/2004 clearly lays down that only operations between ‘previously independent undertakings’ can be concentrations. Thus, in the EU system, intra-group restructurings are definitely not concentrations. On the contrary, its analogous Chinese provision, Article 20 of the AML, does not directly resolve this issue and leaves it to Article 22 of the AML which merely exempts intra-group operations from compulsory notification. Intra-group operations are defined as cases in which:

- (1) one business operator who is party to the concentration has the power to exercise more than half of the voting rights of every other business operator, whether of the equity or the assets; or
- (2) one business operator who is not a party to the concentration has the power to exercise more than half of the voting rights of every business operator concerned, whether of the equity or the assets.

At first sight, we may think that there may be no significant difference in practical terms between the Chinese and the EU system at this regard: in both cases, intra-group operations are not subject to mandatory notification. However, from a conceptual perspective, it would have been much more coherent to fully exclude intra-group operations from the concentration category and not only exempt them from the mandatory notification. Moreover, it is not clear that the 'content' of the intra-group exemption is going to be interpreted in identical terms in both legislations. The AML's definition is simpler than the EU's notion and thus it may not catch exactly the same transactions.

Other exceptions to the concentration concept contained in Article 3.5 of Regulation 139/2004 (public mandate in insolvency proceedings or certain acquisitions by financial entities provided they only exercise their voting rights temporarily and only to prepare the sale or protect the investment) had no analogous provisions under the AML; however, as there are very good reasons to exclude them from the mandatory notification obligation, the Chinese system should end up following a similar path.

Notification of a concentration is only mandatory when the concerned parties' turnovers exceed certain thresholds, as laid down in the Notification Thresholds Rules, in particular:

The total worldwide turnover of all parties to the transaction exceeded RMB 10 billion and the PRC turnover of each of at least two parties to the transaction in the previous financial year exceeded RMB 400 million; or

The combined PRC turnover of all parties to the transaction exceeded RMB 2 billion and the PRC turnover of each of at least two of the parties to the transaction in the previous financial year exceeded RMB 400 million¹³.

The design is therefore based on 'turnover thresholds' –as in the EU system– and not on other criteria such as market share of the parties which would make much more difficult to know if the concentration has to be notified. The disadvantage of 'turnover thresholds' is that many concentrations without anticompetitive concerns may be subject to mandatory notification. This is why a simplified notification and an expedited procedure are usually made available for these cases¹⁴. However, up to now China has not yet provided these simplified mechanisms. It is true that, for this starting stage, the thresholds might have been set at a high level –at least for Chinese businesses standards– so as not to catch too many concentrations but it is also true that many restructurings with no anticompetitive concerns will still be subject to mandatory notification. It would be helpful to see in the next future the development of brief notification forms and of possibilities for applying for an exemption of a full standard filing.

Regarding foreign mergers, these will also fall under the Chinese merger control if they exceed the corresponding thresholds, regardless of whether the parties concerned do or do not have subsidiaries or branches domiciled in China¹⁵. It would not be difficult for a foreign merger to exceed the thresholds. The worldwide turnover of RMB 10 billion (equivalent to around 1 billion Euros) is far lower than the worldwide turnovers used in the European Union (5 or at least 2.5 billion Euros). Thus, this first threshold will be reached by many more and smaller foreign companies than in other jurisdictions such as the EU. On the other hand, the second threshold represents an intention to exempt concentrations of companies with no business or no significant business in China. However, the threshold is again fixed at a low level: at least each of two of the parties concerned must have a PRC turnover of RMB 400 million (equivalent to around 40 million euros) which is also much lower than the 250–300 million Euros required in the EU. Although the EU and China's situations are not fully comparable, 40 million Euros in the huge Chinese market does not seem a very high amount, in particular for EU or American companies already fulfilling the first threshold criteria. This is even more the case if we consider that, as in the EU case, the thresholds are equally applicable to all type of concentrations –horizontal, vertical and conglomerate mergers– and the turnover included will likely be the whole group's turnover. In summary, many foreign-to-foreign operations will be caught by Chinese merger control. The same is true for acquisitions of Chinese businesses by foreign investors.

Voluntary notification or/and *ex officio* examination of concentrations below the thresholds is also possible. Indeed, Article 4 of Decree No. 529 states that investigations shall be carried out by the authorities when a concentration below the thresholds 'has or may have the effect of foreclosing or restricting competition'. This provision is likely intended to permit control of concentrations below the thresholds between parties with very high market shares and to be used only in very extraordinary cases. However the mere existence of this provision introduces uncertainties as to which concentrations should be notified and opens the door to *a*

posteriori control of certain mergers following complaints and/or pressures of competitors and other private or public bodies¹⁶.

A reportable concentration shall not be closed and implemented until it has been notified and authorised by the Chinese authorities¹⁷. Thus the projected concentration is temporarily suspended until a decision is taken. The AML does not contain explicit possibilities of lifting of suspension or applications for a lifting of suspension as foreseen in other jurisdictions¹⁸. If these notification and suspension obligations are not respected, the authority shall order cessation of implementation of the concentration, disposal of shares or assets, transfer of the business or any other restorative measure within a given time limit and may impose a fine of a maximum of 500,000 RMB (around 50,000 Euros)¹⁹.

The review process is structured in two stages. Phase one implies an initial waiting period of 30 days, not starting on the notification date but when that notification is deemed to be complete. The filing requirements and their level of detail are similar to the ones required in other jurisdictions. Within the 30 days preliminary review the authorities will decide either to conduct further review (a second phase is opened and the suspension of the concentration is extended) or to authorize the concentration. If they fail to take a decision within the time limit, the concentration may be implemented (positive silence)²⁰. The second phase shall be completed within 90 days of the date the decision to conduct a further review was taken although an extraordinary possibility of extending the deadline is foreseen²¹. The authorities shall then decide to prohibit the concentration or to authorise it, either with or without conditions attached²². Once again, if they fail to take a decision within the time limit, the concentration may be implemented (positive silence)²³.

Another relevant issue is that only decisions prohibiting a concentration or clearing it with conditions have to be made public. Notifications do not need to be publicly announced –not even a brief summary of the notification for interested parties–, either in the case of phase one decisions (to conduct further examination or to authorise the concentration) or phase 2 decisions clearing the merger without conditions. Moreover, it will also be important to see the level and extent of reasoning of the public decisions²⁴.

The basic design of the review process and its duration do not substantially differ from other jurisdictions such as the EU. It still remains to be seen whether the rules are also applied in a similar way. Particular attention shall be paid below to the application of the start–the–clock requirement (the timing to decide that the notification is complete) and of the exceptional circumstances for extending the deadlines. These two aspects jointly with the level of detail of the decisions reasoning and the respect of the parties' rights of defence will be key to assess the review procedure and in particular its speed/effectiveness, transparency and fairness.

2.2. The decision on the merits: the criteria to prohibit or clear a concentration

While the EU merger control system seems to lay down a 'pure competition test' for the 'competition review' and the decision whether to prohibit or clear a concentration, the AML is not so clear and seems to leave the door more open to other kinds of considerations –e.g. industrial policy– even within the 'formal competition review' and not only under other more appropriate review procedures such as the 'foreign entry review' or the 'national security review'. Taking into consideration the design of the 'test' envisaged by the AML and the Chinese context, there is a high risk that industrial policy considerations will invade and vitiate the pure competition review in China and, consequently, increases uncertainty, a lack of transparency and even accusations of discriminatory treatment, undermining therefore the necessary credibility of the Chinese merger control authorities.

In order to explain these risks, the analysis will first be focused on pure competition aspects (e.g the main substantive 'competition test', the possibility to invoke the efficiency or the failing firm defence and possible references in the AML to other antitrust concerns such as how to treat spill–over effects in joint venture cases or ancillary restrictions) and then it will move to other non pure competition concerns.

2.2.1. The main substantive 'competition test'

The AML defines the main substantive competition test in Article 27 by stating:

'Where a concentration has or may have the effect of eliminating or restricting competition, the Antimonopoly Authority under the State Council shall take a decision to prohibit the concentration'²⁵.

It is important to stress that, according to this provision, not only the actual or potential elimination of competition in the market but also a simple ‘restriction’ of competition (actual or potential restrictive effect) could be sufficient to prohibit the concentration. The legal test is very broad: almost all horizontal mergers and many vertical and even conglomerate mergers in neighbouring markets will likely have these actual or potential restrictive effects and may fall under the prohibition.

The very broad character of this test becomes more visible when we compare it with the tests used in the EU and the USA. For instance, Article 2, paras. 2 and 3 of the EU merger control regulation lay down that a concentration will never be forbidden unless it ‘significantly impedes effective competition in the Common Market, or a substantial part of it, in particular as a result of the creation or strengthening of a dominant position’²⁶. This provision is setting up a much higher threshold for prohibiting a concentration: not ‘any’ restrictive effect of the concentration is sufficient, but rather only a ‘significant’ obstacle to ‘effective’ competition. The example of that significant obstacle used in Article 2 (a creation or strengthening of dominant position) reinforces the idea that the effect must be very substantial. Moreover the test was immediately explained in detail in the Commission Guidelines for the assessment of horizontal concentrations²⁷. Article 2 in itself (reinforced afterwards by the Guidelines explanations) substantially limits the discretion of the European Commission to prohibit a merger. It is also relevant to say that the current test was only introduced by Regulation 139/2004. Before then, the test was even clearer and more limited in scope: only concentrations creating or strengthening a dominant position could be forbidden²⁸. Thus, the set up of EU merger control was simultaneous with strong guarantees to undertakings concerning which concentrations will never be forbidden.

Coming back to China, it is quite obvious that the Chinese authorities do not intend to prohibit mergers having ‘any’ restrictive effect (as explained earlier, that will lead to prohibiting almost all horizontal mergers and many vertical and conglomerate mergers) but it is also very clear that they have intentionally preferred a very broad legal test, giving them a wider discretion to examine the concentration and consequently introducing more uncertainties for undertakings. This wide discretion is problematic and should be resolved as soon as possible. If a change in the Law is not foreseeable in the next future, the need for general guidelines and clear/detailed reasoning of individual decisions is absolutely vital in order to reduce discretion and promote transparency and legal certainty for economic operators. The recent Provisional Merger Assessment Rules are a good step in this direction but further and more detailed steps are still needed.

The AML, in Article 27, only gives initial very general guidance on the factors that should be taken into account for the competition review, including the market share of the companies concerned, the effects of the concentration on market access and technological progress, on the consumers and business operators (competitors and third parties) and on ‘national economic development’. The list is not exhaustive²⁹. With the exception of the last factor (‘national economic development’), all the rest are typical factors included in merger control rules in most jurisdictions³⁰.

Although ‘economic development’ is not an unusual factor in many jurisdictions, it is not at all common to refer to ‘national economic development’. In the EU, for instance, Article 2, 1, b) of the Merger Control Regulation allows consideration of the contribution of the concentration to technological or economic development (not European economic development) and only provided that this development benefits consumers and does not constitute an obstacle to competition. These differences in the Chinese system have given rise to suspicion regarding the possibility of using non pure competition factors in the competition review³¹.

2.2.2. Efficiencies and other ‘competition defences’. Some significant lacunae regarding the competition review

According to Article 28 of the AML a concentration having restrictive effects on competition may, however, be permitted ‘if the business operators concerned can prove that the concentration will bring about a more positive than negative impact on competition [...]’. This sentence seems to open the door to the use of the ‘efficiencies defence’ and also to a certain extent the so-called ‘failing firm defence’.

The efficiencies defence was first explained within the EU Merger control system in the Guidelines for the assessment of horizontal concentrations³². It allows the undertakings concerned to invoke and give evidence of actual or potential efficiencies originated by the concentration that could benefit consumers and could compensate the negative effects of the concentration. Only efficiencies that are inherent to the concentration,

and could not thus be obtained through other less restrictive means, could be admitted³³. It is for the European Commission to then assess the balance between negative and positive effects of the concentration and take the final decision. In view of the high threshold established in order to prohibit a concentration, the efficiencies defence has had a limited role in the EU up to now, although it has been more often invoked recently. It is still to be seen how this exception will be interpreted in China and which role it will play. Just by looking at the AML, there might be more scope for the use of this efficiencies defence as the threshold in order for a concentration to be prohibited is set up by the AML at a lower level.

Within the EU system, the failing firm defence is also systematically explained in the Guidelines for the assessment of horizontal concentrations³⁴. It can be used when one of the parties to a concentration is a failing firm (an undertaking that, due to its economic problems, will be obliged to abandon the market in the near future if it does not merge) and only provided two additional conditions are fulfilled: first, no other less restrictive realistic alternative to the merger exists; and, second, should the merger not take place, the failing firm's assets will disappear from the market. In summary, the exception is subject to very strict conditions: in practice, the European Commission has to be convinced that the damage to the competitive structure of the market is not a consequence of the concentration because, even if it does not authorise the acquisition of the failing firm, the damage will take place and will be equal or higher than in a clearance scenario. Although not explicitly mentioned, nothing in the AML impedes the use of a similar failing firm defence in China. Firstly, because if the same conditions as in the EU are applied, the concentration is not having the effect of eliminating or restricting competition in the sense of Article 28 AML and therefore should not be forbidden; and secondly, because, applying the second sentence of Article 28 AML, the concentration scenario might be better (positive impact) than the non-clearance scenario. Indeed, the recent Provisional Merger Assessment Rules explicitly mention the possibility of a 'failing firm defence' although they do not provide with detailed guidance on when it will be available.

Two relevant lacunae regarding the substantive review can be seen in the AML:

– The first one relates to the analysis of spill-over effects in joint venture cases. Within the EU, joint venture cases falling under merger control are subject to two substantive tests: the core of the operation (markets where the parties merge their activities) is examined under the usual main substantive test for mergers, that is to say the 'significant obstacle to effective competition test'³⁵, while the impact of the concentration on independent activities of the parties, either in the joint venture's market or other related markets (vertically related markets or neighbouring markets), is subject to the substantive test contained in Article 101.1 and 3 of the Treaty on the Functioning of the European Union (hereinafter TFEU), that is to say the 'appreciable restrictive effect test' of Article 101.1 TFEU and the 'balance test' between positive and negative effects of Article 101.3 TFEU³⁶. The crucial issue is that there is a concern regarding the impact of the concentration in both the merger markets and other related markets where the parties maintain independent activities and they may coordinate their behaviour as a consequence of the concentration. Both aspects are subject to different tests although within a single procedure.

In China, the AML contains no specific reference at all regarding the analysis of joint venture cases. As many joint ventures will fall under merger control, we should presume that, in principle, the same substantive test as for other mergers is applicable. However, there are uncertainties on whether and how spill-over effects in other related markets will be examined. It is also true that nothing in the AML impedes this examination. In any event, all these aspects deserve detailed development in future guidelines.

– The second lacuna concerns the so-called ancillary restrictions, that is to say restrictive clauses (e.g. non-competition clause, supply obligations, etc) attached to the concentration, subordinated in importance to the main operation, directly linked and indispensable to the concentration. In the EU system, these restrictions will form part of the global assessment of the concentration and will be covered (even if no explicit mention is made) by the clearance decision³⁷.

The AML lacks a reference to ancillary restrictions. We do not know whether they will be examined with the main operation, under a single procedure and by the same authority. More importantly, we do not know if ancillary restrictions are covered by clearance decisions. Once again, it is important to take all these aspects into consideration and try to fix them in future guidelines. Although the AML makes no explicit reference to ancillary restrictions, nothing in the AML impedes the Chinese authorities from in the end following a similar path to deal with ancillary restrictions.

2.2.3. Conditions and remedies to deal with (antitrust) concerns

In most jurisdictions, prohibitions of mergers are very exceptional. More than prohibiting a merger, the competition authorities tend to favour conditional clearances (approvals subject to certain conditions) and/or the proposal by the parties concerned of 'remedies' to the antitrust concerns identified by the competition authorities.

This is also true regarding the EU system where only a few mergers have been prohibited and, on the other hand, many have been approved after the parties and the Commission have agreed on remedies to deal with antitrust concerns. In the EU, these remedies can be proposed by the parties both in the first and second phase of the procedure³⁸.

In China, the AML also foresees the possibility of conditional approvals in Article 29 when it states that 'Where the concentration is not prohibited, the Anti-monopoly Authority [...] may decide to attach *restrictive conditions* for reducing the negative impact of such concentration on competition'. Although there is no explicit reference in the AML to remedies, it was clear from the beginning that this possibility of 'restrictive conditions' was de facto opening the door to the parties to propose remedies and negotiate a conditional approval with the Chinese competition authorities. All this was formally confirmed by the adoption of the Concentration Review Rules in 2009³⁹. The main features of this remedies system are the following:

- (1) It is definitely confirmed that the parties to the concentration can provide 'restrictive conditions' (remedies, in the usual terminology in other jurisdictions) by adjusting their concentration transaction plan⁴⁰.
- (2) There is no doubt that these remedies can be proposed by the parties during the second stage of the procedure, once MOFCOM has raised objections to the projected concentration. However, the proposal of remedies during the first stage of the procedure is not ruled out. On the contrary, Article 11 of the Concentration Review Rules says that remedies can be provided 'during the examination process', without limiting this possibility to the 'further examination stage' mentioned in Article 10 or excluding this possibility in the 'primary examination stage' referred to in Article 9.
- (3) Remedies can be structural (e.g. divestitures⁴¹), behavioural (e.g. 'granting access to such infrastructures as network or platform, licensing of key technologies and termination of exclusive agreements') or hybrid (combination of both).
- (4) Remedies shall be 'clear and definite enough to evaluate their effectiveness and feasibility' and they 'shall be able to eliminate or reduce the effects of precluding and restricting competition'⁴².
- (5) Interestingly, remedies and conditions seem to be limited to avoid pure competition concerns. Article 29 AML is clear enough when it states that the restrictive conditions may be attached 'for reducing the negative impact of such concentration on competition'. With similar words, Article 11 of the Concentration Review Rules lays down that remedies may be provided 'in order to eliminate or reduce the effects of precluding and restricting competition'. Theoretically at least, other non competition concerns will not be addressed through these remedies.
- (6) Article 13 of the Concentration Review Rules seems to suggest that there is significant leeway for informal negotiation between the parties to the concentration and MOFCOM regarding the acceptable remedies/conditions.
- (7) Unlike in the EU system, MOFCOM seems to have a wider scope for departing from remedies proposed by the parties and imposing on the parties conditions unilaterally decided or amended.
- (8) Undertakings are obliged to report on the implementation of the conditions according to the prescribed schedule, MOFCOM is entrusted with the supervision of remedies/conditions compliance and where a failure is detected, MOFCOM will also order the correspondent corrections and/or take all the other appropriate measures to solve the situation⁴³. Regarding divestitures in particular, the Provisional Rules on Divestiture require the parties to preserve their value and provide information and assistance to prospective buyers; they also require the appointment of a trustee to monitor the entire divestiture process (an if the parties cannot find an appropriate buyer, they can require another trustee to do it)⁴⁴.

2.2.4. Beyond a pure 'competition review': industrial policy and the national interest

This is by far the most controversial issue of the Chinese merger control design: to what extent the competition review in China allows or even promotes consideration of not purely competition concerns but also other type of concerns such as industrial policy or national interest concerns?; and consequently to what extent the AML, instead of introducing a mechanism to promote a level playing field – a set of rules equally applicable to national and foreign companies operating in China– generates on the contrary a risk of discriminatory treatment?

Let us start by saying that China, like other jurisdictions, has certain legal mechanisms to avoid harm to national security and to control foreign investment. There is a Chinese 'national security review' and a Chinese 'entry review or foreign investment review'. This paper does not deal in detail with these mechanisms and focuses mainly on the competition review of mergers⁴⁵. The key question here to be examined is whether, within this competition review of mergers, not purely competition concerns can play a role. A good number of provisions of the AML open the door to this possibility or at least create doubts regarding this possibility, in particular the following:

Article 27 AML includes within the factors to be considered for the competition review of mergers the effect of the concentration on 'national economic development', an expression that many commentators interpret as the effect of the concentration on Chinese industry (companies, trademarks, research & development, etc). To a certain extent, the expression opens the door to consider not only if the concentration is 'good for consumers or effective competition in China' but if the concentration is also 'good for China' (understood as China's industrial or political interests).

Article 28 AML allows the Chinese authorities to clear an otherwise prohibited concentration if it is 'pursuant to public interests'. Significantly, this provision does not allow, even if it is pursuant to the public interest, the prohibition of a concentration that does not restrict competition or the imposition of conditions before authorising a concentration that does not raise antitrust concerns. Note, however, that the formal legal substantive test regarding prohibition of a concentration (actual or potential restrictive effect) is, as explained above, set very low.

Article 31 AML indicates that for concentrations in which one of the parties is a foreign investor, 'if state security is involved, besides the examination on the concentration in accordance with this Law, the examination on national security shall also be conducted in accordance with the relevant State provisions'. This provision might be interpreted as just recalling that certain foreign investments may have to pass an additional review (the national security review). However, due to the possibilities offered by Article 27 and 28 AML that we have just mentioned, it also generates doubts on whether national security concerns could or should also be considered within the competition review (as part of the public interest or national economic development issues).

Article 5 AML foresees that 'Business operators may, through fair competition and voluntary alliance, concentrate themselves according to law, expand the scope of business operations and enhance competitiveness'. This provision is understood to reflect the state's policy of encouraging consolidation and concentration of Chinese domestic companies –particularly State owned companies– and promoting successful national champions to compete with foreign multinational companies⁴⁶.

Article 7 AML addresses in general the application of the AML to State owned enterprises –hereinafter SOEs– creating important doubts on whether they are subject in full to the AML.

Finally, some of the previous provisions are reinforced more in general by Article 1 AML which states that the aims of this Law are not only to prevent and restrain monopolistic conducts, protect competition in the market, enhance economic efficiency and safeguard the interests of consumers but also 'the social public interest and promoting the healthy development of the socialist market economy'; aims that may be contradictory and that therefore allow more discretion to the authorities and increase uncertainties for the operators concerned.

It is fair to say that all this package, jointly with the low threshold laid down in Article 28 in order to prohibit a concentration and the lack of clear and detailed guidelines on the substantive assessment of mergers, have generated a lot of criticism, a great degree of uncertainty and even suspicions of discriminatory treatment for certain acquisitions, thus risking the undermining of the credibility of the competition merger review process and more in general the credibility of the Chinese merger control authorities⁴⁷. Only a consistent and publicised

practice, detailed general guidelines and a clear separation between the competition review (with only pure competition concerns analysis) and other type of reviews (entry and national security review) could improve this design and eliminate or reduce the aforementioned risks. The analysis of the first years' practice is precisely the object of the following section.

3. China's merger control in practice (August 2008–October 2011)

3.1. Preliminary comments on public information and transparency

An analysis of Chinese merger control practice has to start by stressing the very limited obligations of publicising of decisions imposed by the AML on Chinese authorities and, in general, the needs for more transparency regarding merger control in practice. However important efforts are being made by the Antimonopoly Bureau (within MOFCOM) to informally circumvent, at least to a limited extent, these pitfalls.

There are no official statistics on Chinese merger control at the MOFCOM's web site and, according to the AML, there is no need to publish any information regarding the notifications received or even unconditional approval decisions. Only prohibitions decisions and conditional approvals have to be published⁴⁸. Up to now, these minimum legal obligations have been followed to the letter in practice and therefore we only have 9 published decisions in the first three years of application of the AML (one prohibition decision and eight conditional approvals)⁴⁹. Furthermore, some of these decisions are very short (half a page) and the reasoning is extremely limited when compared with other more mature jurisdictions. Nor there is an annual report of MOFCOM explaining data and key features on the application of merger control. Most of the general information on merger control application has been made available through press conferences and/or press releases or through interviews of high-level civil servants by the media or specialized press. Insights offered by law firms and economic consultants with offices in Beijing have also become an important source of information.

In other jurisdictions such as the EU, the publication obligation is much wider in scope, obliging the European Commission to publish all substantive decisions of second phase cases plus all decisions to fine⁵⁰. All these decisions are published in all official languages of the EU. Brief information on every notification received is also officially published so that all interested third parties can know and comment on the merger project. Moreover the European Commission, on a voluntary basis and since the very beginning of EU merger control, has been publishing on its official web site all merger control decisions, including final first phase decision, although they are only published in one language and tend to be less detailed. Transparency and self-discipline are reinforced, *inter alia*, by implementing regulations and by very detailed guidelines on jurisdictional/procedural issues and on the substantive assessment of concentrations (both horizontal and non-horizontal concentrations). Furthermore, the web site regularly updates statistics on merger control and an annual report is published on the application of every main block of EU Competition law, including merger control. Speeches, press conferences and press releases together with a regular newsletter published by DG COMP (European Commission) are also very useful tools to increase transparency.

Starting the enforcement of the AML is not an easy task, particularly taking into consideration the lack of previous experience and the Chinese context. It is logical to assume therefore that the standards of transparency could not be the same as in more mature jurisdictions, at least during the first years of enforcement. However, transparency is crucial in order to have a clear understanding of policy enforcement and should be progressively reinforced in China. Without an appropriate level of transparency, there is significant risk of misunderstandings and even of undermining of the potential of policy improvement and credibility of the authorities.

3.2. Basic statistics

As of October 2011, MOFCOM had received more than 240 notifications of proposed concentrations⁵¹. Most of them, more than 95%, were unconditionally approved. Only around one-third appeared to have been formally approved within the 30 initial days of the first-phase review, although in many cases extensions did not reflect substantive concerns but were due to resource constraints or to delays in the 'final sign-off' by senior MOFCOM officials outside the Anti-Monopoly Bureau⁵². However, it is important to stress that, as in the EU, most of the deals are still expected to be cleared within the Phase-One review, according to public statements from the Anti-Monopoly Bureau officials. The remaining cases were either withdrawn by the parties or subject

to more detail scrutiny. In 9 of those cases a final decision was published: in only one case, prohibiting the concentration, the Coca-Cola/Huiyuan decision⁵³, and in the other eight cases (InBev/AB, Mitsubishi/Lucite, GM/Delphi, Pfizer/Wyeth, Panasonic/Sanyo, Novartis/Alcon, Uralkali/Silvinit, Alpha V/Savio), approving with conditions the proposed acquisitions⁵⁴.

A comparison between the first, second and third year of enforcement may be useful to reveal some trends. In the first year around 60 cases were notified, 52 cases were reviewed, one acquisition was prohibited (Coca-Cola/Huiyuan) and two acquisitions were subject to conditions (InBev/AB and Mitsubishi/Lucite). In the second year of enforcement, the number of notifications significantly grew up to more than 80 cases (a 25% increase), no acquisition was prohibited and 3 were approved with conditions (GM/Delphi, Pfizer/Wyeth, Panasonic/Sanyo). In the third year, the number of notifications grew up again to around 100 cases (a new 20–25% increase), no acquisition was prohibited and 2 conditional clearances were issued (Novartis/Alcon and Uralkali/Silvinit) with an additional decision on the Alpha V/Savio case taken in October 31 2011.

The clearance rate is very high: above 99%, if we consider that only one prohibition decision has been issued out of more than 240 notifications; around 95% of unconditional clearances (only 9 cases of prohibitions/conditional clearances out 240 notifications), although a bit less than 95% if we add to those 9 cases some withdrawals which would have very likely encountered objections by MOFCOM.

3.3. Key jurisdictional & procedural issues

Two blocks of key issues will be examined: firstly, those regarding the crucial issue of ‘timing’ (including pre-notification discussions, completeness of formal notification, first and second-phase practice, respect of time-limits and exceptional extensions and finally possibilities of expedited procedure or abbreviated filing); secondly, those concerning jurisdictional issues and compliance with mandatory notification (including minority shareholding and joint ventures notifications, filing practice and fining policy in the event of violation of mandatory notification).

3.3.1. Timing

As explained in detail earlier, the first-phase review should be conducted in 30 calendar days from the date the notification is deemed to be complete and, in the event a further investigation is needed, a second-phase is opened that should be conducted within 90 calendar days, although this last time limit may be extended in exceptional circumstances⁵⁵. In total therefore, the decision should be taken within a time-frame of 120 days (180 in exceptional circumstances) from formal notification. Practice has revealed that:

MOFCOM welcomes and promotes pre-notification meetings. It is advisable to go early to the Anti-Monopoly Bureau and allow time for extensive pre-notification discussion. These pre-notification meetings have been crucial for consulting jurisdictional doubts. Some clearances (even conditional clearances) have been obtained in a short time, as first-phase decisions but after extensive pre-notification discussions (e.g. InBev/AB or GM/Delphi).

The start-the-clock moment is still more uncertain than in other more mature jurisdictions. MOFCOM has wide discretion when deciding when the notification is complete and the formal review (and the time limits) only starts from the date notification is deemed complete. It has not been unusual for additional information to be requested from the parties (even several times) before formally opening the first phase. Regarding the 9 decisions published, the period between the initial submission by the parties and the start-the-clock decision by MOFCOM has varied from very short periods of one or two weeks (such as in the GM/Delphi and the Pfizer/Wyeth cases) to around one month (Coca-Cola/Huiyuan, Mitsubishi/Lucite or InBev/AB), to almost two months (Alpha V/Savio) or to more than 3 months (Panasonic/Sanyo and Uralkali/Silvinit). It was encouraging to know that in Novartis/Alcon, MOFCOM accepted the case on the same day as it received the notification. Even if it is very likely that draft versions of the notification were supplied in pre-notification meetings, this practice contrasts with past cases.

According to public statements of the Anti-Monopoly Bureau officials, most of the transactions were expected to be cleared within the phase one review. However, only one-third have been formally approved within the 30 initial days of the first-phase review, although in many cases extensions did not reflect substantive concerns but were due to resource constraints or to delays in the ‘final sign-off’ by senior MOFCOM officials outside the Anti-Monopoly Bureau.

If antitrust concerns arise and remedies are needed, examination will very likely enter the second phase. Around one-third of the transactions notified have entered the second phase⁵⁶. These numbers are extremely high in comparison with other jurisdictions and there is room for future improvement.

Once the second phase is initiated, extraordinary extensions of the 90 calendar days' time limit have not been the general rule, although that possibility was used in the Panasonic/Sanyo case. The extension was requested by the parties and was needed to reformulate the remedies proposed. On the other hand, some second phase cases had finished almost a month or even two months before the deadline (e.g. Mitsubishi/Lucite and Uralkali/Silvinit respectively).

The overall timing (starting from the initial submission by the parties, not the complete notification and excluding pre-notification meetings) for the 9 published cases goes from the 2.5 months of the InBev/AB case to the 9.5 months of the Panasonic/Sanyo transaction. However, most of these second-phase cases were solved within 5–6 months from the initial submission (Coca-Cola/Huijuan, Mitsubishi/Lucite, Pfizer/Wyeth, Novartis/Alcon, Uralkali/Silvinit and AlphaV/Savio). Note again that there were pre-notification meetings in many of these cases.

Although there is not yet an expedited procedure or a short form filing, latter practice appears to reveal that MOFCOM is becoming more willing to waive certain filing requirements if parties prove that the information required is extraneous or unduly onerous for the parties concerned, particularly if the transaction does not have a significant impact on Chinese markets⁵⁷.

In summary, it is very welcome that Chinese authorities have been able to decide, even complex cases, within a relatively reasonable timeframe. Notifying companies have thus indicators that their case will be decided within a short and relatively reasonable time-frame. This is extremely important from both national and international merger control perspectives. However, uncertainties on the start-the-clock moment should be progressively clarified and less cases should be decided in the second phase. China must progressively change its image of being too often the last important jurisdiction to clear a transaction. An expedited procedure or short form filing would also be convenient in the next future. Until this possibility is approved, the increased flexibility shown by MOFCOM towards waiving certain filing requirements must also be welcome.

3.3.2. Compliance with mandatory notification and some key jurisdictional issues

Has the enforcement of merger control clarified the jurisdictional uncertainties left opened by the text of the AML, mainly regarding the concept of concentration? Has practice revealed full compliance –or at least a high level of compliance– with mandatory notification? Has MOFCOM acted against firms disregarding their notification obligation? Is voluntary notification or *ex officio* examination playing a role in Chinese merger control? These are the key questions to be answered in this section.

Firstly, many uncertainties still remain regarding jurisdictional issues and in particular the scope of the concentration concept. At least the 9 published decisions have not resolved the big questions left opened by the AML⁵⁸. It is true that it seems that Chinese merger control has only dealt, to our knowledge, with durable changes of control, but it would be important to set aside other possibilities with a clear public pronouncement in this connection by MOFCOM.

Regarding the extent to which joint ventures are subject to merger control, MOFCOM seems to take the view that joint ventures (regardless of whether they are full-function or not) should be notified⁵⁹. This is consistent with pre-AML practice under the Chinese M&A guidelines for foreign mergers, but not with other international merger control practices such as the EU and USA systems⁶⁰. This interpretation is also more consistent with the current Article 20 of the AML which does not made any specific reference to joint ventures: it just requires an acquisition of control or decisive influence without making any exception for partial-function joint ventures.

In relation to minority acquisitions, the 9 published decisions have offered no clear guidance on whether they will be caught by merger control⁶¹. Until implementing guidelines provide further explanations, a lot of uncertainties still remain. Previous draft guidelines laid down that control was obtained when the acquirer gained the ability to decide some strategic decisions (appointment of management, budget, operations and sales, substantial investment and other management and operational strategies), but this guidance was removed from the final text. This removal has reinforced uncertainties, particularly because it may be revealing

a continuing debate within MOFCOM and associated agencies about which deals should fall under merger review⁶². Up to now, practice suggests that the acquisition of a veto over certain strategic decisions could suffice to acquire control, just like in the EU. But no clear guidance is offered on it and in particular it does not clarify if other minority acquisitions could also be caught by merger control.

In both cases –joint ventures and minority acquisitions–, it is better to be cautious and either to notify or at least to clarify possible doubts through pre-notification meetings with the Chinese authorities. Detailed jurisdictional guidelines regarding the concept of concentration would be very welcome. From the evidence so far, it is possible that China ends up applying a more expansive concept of concentration than the EU and therefore more extensive notification duties.

Secondly, with regard to the level of compliance of the duty to make prior notification of concentrations, the enforcement record seems to suggest that the level of compliance is increasing (this might be one of the factors explaining the 25% increases of notifications between 2009 and 2010 and again between 2010 and 2011). There are contradictory opinions regarding the level of compliance: while Chinese authorities defend that a rather high level of compliance is being attained, other actors suggest the opposite opinion⁶³. Anyhow, there is still a cause of concern regarding domestic firms, in particular SOEs. MOFCOM has indicated that not only domestic firms but also SOEs are subject to merger control review, but the truth is that some SOEs seem to have been reluctant to notify their transactions: it has been reported for example that no filing was made regarding the October 2008 merger between two of China's leading telecommunications companies, China Unicom Limited and China Netcom Group corporation Limited⁶⁴. The merger was governmentally approved –in particular by China's Ministry of Industry and Information Technology– but was not subject to review by MOFCOM under the AML. It might be therefore that these types of cases provoke an inner battle between different government branches. If such cases are repeated and escape competition review, it might seriously undermine the neutrality and credibility of the merger control system.

Until now, no fines have been imposed for violation of mandatory notification. The reasons for this could be that the level of compliance is high, that there are still important jurisdictional uncertainties and that SOEs have not always fully complied with notification duties. This absence of fines during the initial period of enforcement has also occurred in other jurisdictions such as the EU and will likely change in the next future⁶⁵. There are not yet any data regarding voluntary notification of concentrations below the thresholds or *ex officio* examinations.

3.4. Key substantive assessment issues

Following the structure of the mirror section above on the substantive assessment of mergers⁶⁶, I will proceed to examine what enforcement practice can reveal regarding, firstly, the application of the core competition test (actual or potential restrictive effect) and other complementary aspects such as efficiencies. Where possible, references will be made to questions such as market definition, market factors used for the assessment (market shares, markets powers, barriers to entry, etc) and theories of harm; secondly, the application of remedies to resolve concerns, including questions such as when remedies have been proposed and imposed (first phase or second phase decisions), type and scope of the remedies used (behavioural, structural or hybrid) and, where possible, soundness of the remedies for dealing with antitrust concerns; thirdly, inquiries on what merger control practice reveals regarding industrial policy considerations and discriminatory enforcement concerns.

3.4.1. Competition test and economic analysis

An analysis of the merger control enforcement (mainly the 9 published decisions) until now suggests the following:

It is encouraging that the reasoning of the decisions, although still extremely brief in comparison with decisions of more mature jurisdictions⁶⁷, are becoming more detailed and, even more interestingly, there seems to be a trend at least to a certain extent, towards the use of more economic analysis while recalling theories of harm commonly accepted according to best international practices⁶⁸. This could be the result, *inter alia*, of MOFCOM's engagement in important capacity-building efforts and extensive training of its staff, in many cases with assistance from competition authorities in more mature jurisdictions.

For example, the appropriate identification of the relevant market is progressively becoming an important issue in MOFCOM's decisions⁶⁹. It is true that some of the definitions, particularly in the first decisions, are not

specific enough and could be criticized⁷⁰ but it should not be neglected that, in all but one of the decisions⁷¹, the relevant markets concerned are clearly identified, both from a product and geographic point of view. Moreover there are indicators that the definition is becoming less simplistic (e.g. geographic markets have been deemed to be not only Chinese but also worldwide in some cases⁷²) and often coincides with the definition of other jurisdictions in the same merger.

Market shares of the merging parties and of other competitors are often cited and used to demonstrate market power. Again, not all the decisions are exemplary at this regard: in particular, a couple of them –InBev/AB and GM/Delphi– do not mention at all the market shares of the parties. The other five decisions do explicitly mention the market shares of the merging parties pre-merger and/or which will be their post-merger combined market share. Many allude also to the market shares of other competitors as one of the key factors in confirming market power. The post-merger combined market share of the parties ranked from nearly 50% to almost 80% or even 100% in these 7 latter cases⁷³. Not surprisingly, in the two cases where the parties' market shares were not mentioned at all, the estimate of these market shares is very low (in InBev/AB, below 13–20 % in China –it is difficult to assess if the situation was very different in some of the regional markets within China– and, in GM/Delphi, below 20%)⁷⁴. Among the other useful factors, the comparison with the market shares held by other competitors is often mentioned⁷⁵, while entry barriers or the IHH index measuring the degree of market concentration have been mentioned once⁷⁶. This suggests that MOFCOM is willing to engage in a more solid economic analysis and to be more transparent. It is true, however, that, just looking at the decisions reasoning, the analysis seems to be too much focused on market shares and should be refined and/or better explained. Too much reliance on market share to presume market power could be criticised, particularly if there is not yet a due procedure allowing a proper rebuttal process⁷⁷. Note, however, that the use of too-simplistic methodologies is explicitly rejected by the Anti-Monopoly Bureau in MOFCOM. According to its Director-General, Shang Ming:

‘In terms of analytical perspectives, the Anti-Monopoly Bureau emphasizes the complete evaluation of all kind of effects, analyzes all possible factors that may induce competitive effects, and avoids the tendency of simplistic structural methodologies. Some outsiders have speculated, based only on information from the notices that MOFCOM has published so far, that MOFCOM is inclined to use such structural methodologies. However this speculation is baseless’⁷⁸.

Furthermore, although MOFCOM has not until now made explicit reference to efficiencies in merger decisions, it is also encouraging that the Draft Horizontal Merger Guidance did explain conditions for recognising efficiencies⁷⁹.

MOFCOM has thus far clarified that it is not only concerned with horizontal restrictive effects, but also with vertical and even conglomerate mergers.

Within horizontal concentrations, several cases have already been dealt with regarding ‘unilateral effects’ in which the main concern was the elimination of competition between the merging parties. This is the case of Mitsubishi/Lucite, Sanyo/Panasonic, Pfizer/Wyeth, Novartis/Alcon (Medicated eye-care products), Uralkali/Silvinit, Alpha V/Savio and very likely also InBev/AB.

In all these cases, except in InBev/AB and Novartis/Alcon, there was a substantial overlapping between the merging parties leading to a post-merger combined market share of the parties ranging from nearly 50% to almost 80% (or even 100%) of the relevant market. This means that the concentration would have also very likely raised concerns in other jurisdictions.

In InBev/AB, market shares were not mentioned at all in the decision. The estimate of the post-merger combined market share in China was around 13% –we do not know if higher percentages existed in some local/regional markets within China–. In Novartis/Alcon (Medicated eye-care products), the post-merger combined market share in China exceeded 60% but the overlapping between the merging parties was negligible because pre-merger Novartis had less than 1% and, furthermore, it had announced the withdrawal of its existing operations within that market. In these two cases, it is likely that the merger would have not raised concerns in other more mature jurisdictions.

On the other hand, in only one case, Novartis/Alcon (contact lens care products) the concern seems to be ‘co-ordinated effects’, that is to say the impact of the merger in the reduction of competition between the newly-merged entity (Novartis/Alcon, holding a 20% market share for contact lens care products in China, 60%

worldwide) and a third competitor in the market (Hydron, holding a 30% market share in China and appointed by Novartis as its exclusive distributor for contact lens care products). There is no much elaboration on this 'co-ordinated effects' theory in the decision because a remedy (in particular, Novartis' commitment to terminate the distribution agreement with Hydron within the next 12 months) dealt with the antitrust concern. In Uralkali/Silvinit, in addition to unilateral effects, the transaction was deemed to increase the risk of co-ordination between major global suppliers of the product concerned (potassium chloride).

In two cases, vertical effect concerns were raised. In GM/Delphi, the antitrust concerns were, on the one hand, the foreclosure of access of GM's rivals to Delphi car parts and, on the other hand, the restrictions on the sales opportunities of Delphi's competitors if GM favoured, in the post-merger scenario, in-house supplies from Delphi. In Mitsubishi/Lucite, as the newly-merged entity will be active not only in the methyl methacrylate market (MMM) but also in two downstream markets, there was a concern on foreclosure of competitors' activities in those downstream markets due to the dominant position acquired by the newly-merged entity in the upstream market.

Finally, the Coca-Cola/Huiyuan case seems to be a prohibition of a conglomerate merger⁸⁰. The relevant product market, according to the decision, is the fruit juice market in China. Although both Coca-Cola and Huiyuan had pre-merger activities in the juice market in China, the post merger combined market share would be, according to all estimates, less than 30%⁸¹. With that market share and taking into account that another competitor, Uni-President, had almost a 20% market share, it would have been very difficult to build a case for a horizontal merger prohibition. In fact, MOFCOM did not seem to be concerned by unilateral or co-ordinated effects in the fruit juice market, but the main concern seemed to be that the merger could allow Coca-Cola to 'leverage' (through product tying or other exclusionary conduct) its presumed dominant position in the carbonated soft drinks market in China (where it had more than 60% of the market) into the fruit juice market. In other jurisdictions, conglomerate mergers are rarely prohibited and in any case it is for the competition authority to give evidence of the eventual foreclosure effect of the concentration. This has not been the case in China, not at least in the Coca-Cola/Huiyuan decision: without detailed analysis and further evidence, MOFCOM appeared to have too easily assumed that Coca-Cola would have been able, post-merger, to engage in vertical foreclosure or leveraging.

The horizontal and vertical/conglomerate competition concerns perceived by MOFCOM seemed to be similar to those of other jurisdictions. In many of the 9 cases herein examined, similar antitrust concerns would also have arisen in other jurisdictions. However, more mature jurisdictions would have not always reached the same conclusions or, at least, only after evidence is found and a thorough examination of the effects is made. This is particularly true regarding the Coca-Cola/Huiyuan case. There may be other minor differences or doubts, as explained above, in relation to In/Bev/AB, GM/Delphi, and Novartis/Alcon (medicated eye care products). Overall, MOFCOM refers to similar concerns as other jurisdictions but sometimes appears to intervene (prohibiting or conditioning clearances) where other more mature jurisdictions would not have done so.

3.4.2. Remedies

In eight out of the nine published decisions, MOFCOM decided to impose conditions on the parties in order to authorise the concentration. In the only prohibition decision case, Coca-Cola/Huiyuan, it is known that there were also negotiations between MOFCOM and Coca-Cola to see if a remedy could solve the antitrust concerns. For whatever reason, no agreement was reached on those remedies and therefore the acquisition was prohibited⁸². All this seems to suggest that, although the Chinese authorities feel strong enough to forbid certain acquisitions (the prohibition in the Coca-Cola case might be seen as a signal in that direction), they are willing to negotiate with the companies concerned and prefer remedies and conditions that respond to their concerns rather than a full prohibition. This approach is welcome: it is encouraging for the merger parties and it is aligned with best international practices.

Negotiations on remedies seem at times be taking place very early on. In some exceptional cases, initial proposals of remedies might have been submitted to MOFCOM during the pre-notification meetings. This allowed some conditional clearances to be adopted as first phase decisions (30 days from formal complete notification). However, most of the cases where remedies had been imposed are second-phase decisions. In fact, in the only case in which an extraordinary extension of the deadlines was requested, the reason for the extension was precisely the need to reformulate revised remedy proposals⁸³.

Regarding the type of remedies, both behavioural and structural remedies are being used by MOFCOM.

Structural remedies such as capacity divestment or full divestiture were used in Mitsubishi/Lucite, Pfizer/Wyeth, Panasonic/Sanyo and Alpha V/Savio.

On the other hand, behavioural remedies were used in other decisions. For instance, in Mitsubishi/Lucite, there was a commitment not to acquire a domestic Chinese producer or build a new production plant in China. In GM/Delphi, MOFCOM's initial concern on Delphi being able to pass to GM sensitive customer information concerning GM's competitors was addressed through a commitment by GM and Delphi to not exchange trade secrets about Delphi's customers; on the other hand, Delphi committed to supply parts to other car producers in a timely and reasonable manner and GM undertook to avoid discrimination among component suppliers in favour of Delphi and not unduly restrict or delays customers of Delphi from moving to other suppliers. All of these commitments were aimed at eliminating or reducing possible restrictive effects (mainly a foreclosure effect) of the vertical merger on GM's and Delphi's competitors. In Novartis/Alcon (contact lens care products), the concern regarding future co-ordination between Novartis and a third competitor (Hydro) which was at the time Novartis's exclusive distributor for contact lens care products in China, was addressed with a commitment by Novartis to terminate the Novartis-Hydro relationship within 12 months of MOFCOM's decision. In Uralkali/Silvinit, a package of behavioural remedies was designed to maintain the status quo in the structure of the relevant market, guaranteeing sufficient supplies to the Chinese market and the maintenance of customary negotiation procedures.

Structural remedies seem to be more often used to deal with unilateral effects of horizontal mergers (in particular where there is substantial overlap between the parties and a high post-merger combined market share)⁸⁴ while behavioural remedies have been mainly used in vertical concerns⁸⁵. However, and to a lesser extent, structural remedies have also been used to deal with vertical effect concerns⁸⁶ as well behavioural remedies to complement and reinforce divestitures in some horizontal mergers⁸⁷.

Most of the aforementioned remedies are common in other jurisdictions and used in a similar way.

In contrast, some other remedies imposed by MOFCOM's are highly unusual from a Western perspective. This is the case for instance of the obligations imposed on InBev not to increase, without prior approval of MOFCOM, its stakes in the Tsingtao and Zhuijiang Breweries (second and fourth largest producer in China) or not to acquire any shareholding in the two other big competitors (China Resources Snow Breweries and Beijing Yanjing Brewery) and to promptly report of changes in the structure of control of InBev or of its controlling shareholders. Similarly, the type of 'no future acquisition and no new plant in China commitment' imposed in Mitsubishi/Lucite or the behavioural package imposed in Uralkali/Silvinit are also not usual in other jurisdictions.

Two additional conclusions may also be drawn from the enforcement practice. Firstly, it appears that sometimes MOFCOM tends to impose remedies in cases where other jurisdiction would have not intervened at all⁸⁸ and secondly, because of giving only limited reasoning for the decisions or the use of presumptions of market power without sufficient evidence or elaboration, remedies sometimes appear to be a pragmatic way to deal with 'just preliminary concerns' or at least 'not solidly tested concerns': if the parties accept remedies, there is no need to elaborate in depth and prove substantial harm to competition⁸⁹. Hopefully, this impression is false and will disappear once more elaborated reasoning of the decisions is published.

Finally, the monitoring of remedies (particularly behavioural remedies) appears to be thus far satisfactory. According to Shang Ming, the Director General of the Anti-Monopoly Bureau, MOFCOM conducted follow-up investigations in this regard and found that the parties have abided by their obligations and that there have not been any complaints so far⁹⁰.

3.4.3. Industrial policy considerations and discriminatory enforcement concerns

As explained above⁹¹, the AML's design generated significant concerns as to whether industrial policy considerations will be part of, or at least interfere with, the pure competition mergers review. The text allowed significant discretion for public authorities and, as a direct consequence, created a great degree of uncertainty. The reaction was a lot of criticism and even a suspicion that there was discriminatory treatment for certain acquisitions; this reaction is not surprising considering the traditional strong influence of industrial policy considerations in the policy-making of China.

Until detailed general guidelines are issued regarding the compatibility assessment, the first years' enforcement practice is key in determining if these significant concerns were justified or exaggerated. It is not a minor question because the credibility of the whole Chinese merger control system is at stake. So what have we learned from the 9 published decisions and more in general from overall enforcement practice?

(1) The enforcement practice thus far has not dissipated the concerns. Why? There are four main reasons:

- (a) Firstly, the nine published decisions, the only cases where the mergers were prohibited or subject to conditions, were all foreign-to-foreign transactions (8 conditional clearances) or the projected acquisition by a foreign company of a Chinese firm and a traditional Chinese brand (the prohibition decision in the Coca-Cola/Huiyuan case).
- (b) Secondly, it is known that some large mergers between Chinese companies have not properly complied with the mandatory notification obligation and nevertheless have not been punished. This might be revealing an internal struggle between different government departments regarding the role to be played by competition policy in the Chinese policy-making scenario.
- (c) Thirdly, the brief reasoning given for the decisions—particularly in the first two cases, InBev/AB and Coca-Cola/Huiyuan—have allowed for speculation on possible hidden industrial policy reasons behind the prohibition of Coca-Cola/Huiyuan and the imposition of certain conditions on some of the other transactions.
- (d) Fourthly, as already explained⁹², although MOFCOM refers to similar concerns as other jurisdictions, it sometimes appears to intervene (prohibiting or conditioning clearances) where other more mature jurisdictions would not have done so (or not to such a large extent).

(2) However, there are also encouraging reasons to think that competition policy is progressively finding its feet within the complex world of Chinese politics and that pure competition review will be, to a large extent, the core—if not the single—focus of the Anti-Monopoly Bureau. Several indicators support this statement:

- (a) Firstly, the Anti-Monopoly Bureau's senior officials have publicly acknowledged that the mandatory notification duties have been violated in cases involving Chinese companies, they have shown frustration with this and they have publicly announced that future cases will be severely punished⁹³. Moreover they have also defended in press conferences a neutral—non discriminatory—application of the AML to all companies, regardless of their nationality. These statements can be seen as a valid first-step towards a desirable neutral application of the law: a clear message to other government departments and to SOEs that all firms are subject to merger control and that, at least to a large extent, all of them will be reviewed under the same standards. It is still to be seen if the Anti-Monopoly Bureau manages to impose its position and effectively discipline firms and other public authorities.
- (b) Secondly, the reasoning given for the decisions is progressively more extensive and is technically improving. MOFCOM is engaged in important capacity-building efforts and extensive training of its staff, in many cases with assistance from competition authorities in more mature jurisdictions. Officials are rapidly gaining experience in the field and becoming more confident. As a result, although they are still extremely brief in comparison with decisions of more mature jurisdictions, decisions are becoming more detailed and, even more interestingly, seem to follow a trend towards the use of more economic analysis and, at least to a certain extent, an alignment with best international practices. This trend towards more sophisticated analysis and disclosure of the results in the decision should continue as it will be crucial to counter allegations of discriminatory treatment and of hidden industrial policy considerations.
- (c) There is a recent trend towards a clearer separation between of pure competition review and other types of reviews (foreign entry review and national security review). An important and recent step in this direction is the endorsement of new rules on the national security review regarding mergers of acquisitions of domestic enterprises by foreign investors⁹⁴. This review will be handed by a joint conference of various governmental departments. The national security review is widely designed to include not only military-industrial and military related enterprises but also farm products, energy and resources, infrastructures, transportation services, key technologies and major equipment manufacturing and responds to concerns such as the impact of the merger on steady national economy growth, basic social living standards and the R&D capacity in key technologies⁹⁵. In view of the large scope of the national security review, one may even wonder whether

there is any need to use industrial policy considerations in the competition review. There is no doubt that this trend should favour the Anti-Monopoly Bureau limiting its review to strict pure competition concerns and should assist in greater alignment with best international practices in the field.

4. Conclusions and policy recommendations

- (1) By now it is already very clear that Chinese Authorities are exercising effective merger control and that China has become a key jurisdiction when deciding if and when an international concentration can be completed. China is on the way to becoming a significant actor in Global Antitrust, particularly in Merger Control. It is therefore very important to maintain close cooperation with Chinese authorities, to help them with technical assistance and to insist on the importance for China's market and for the international economy of building up a solid, transparent, legally certain and non-discriminatory merger control.
- (2) Like other jurisdictions, the clearance rate in China is very high, above 95%: only one prohibition decision and 8 conditional clearances out of more than 240 cases. These data reveal that the Chinese authorities feel strong enough to forbid certain acquisitions (the prohibition in the Coca-Cola case might be seen as a signal in this direction) but that they are willing to negotiate with the companies concerned and prefer remedies and conditions responding to their concerns than a full prohibition.
- (3) It is welcome that Chinese authorities have been able to decide, even complex cases, within a relatively reasonable time-frame. The average for the 9 more difficult cases has been 90–120 days from the date the notification was deemed complete. Even if sometimes the Chinese authorities took 2–3 months to accept that the notification was complete, notifying companies have now clear indicators that their case will be decided within a rather reasonable time-frame. This is extremely important from both national and international merger control perspectives. However, China is very often the last jurisdiction to clear the transactions and there is room for improvements.
- (4) Important uncertainties and concerns remain regarding the concept of concentration, in particular about the extent to which minority acquisitions and joint ventures should be notified. Guidance should be given by Chinese authorities either by publishing individual decisions or, preferably, by adopting general guidelines. As the concept of concentration is a jurisdictional issue – a key factor in knowing whether prior notification is compulsory – companies must have sufficient information in advance.
- (5) In general, horizontal and vertical competition concerns perceived by Chinese authorities seemed to be aligned with best international practices, maybe with the exception of the Coca-Cola case. However, detailed guidelines are needed, particularly considering the very broad scope of the substantive test included in the AML. The recent Provisional Merger Assessment Rules are welcome but more detailed guidance would be helpful. It is crucial to give a more developed and sophisticated reasoning within the published decisions.
- (6) Remedies and conditions are quite common. Conditional clearances (8 decisions) are preferred to full prohibitions (1 decision). Thus, remedies and conditions have a very important role to play. Both structural and behavioural remedies have been accepted. Notwithstanding the need and the scope of some of the remedies have been quite controversial.
- (7) There are strong concerns about the neutrality of Chinese merger control with suspicions of strict supervision being applied mainly to foreign operations and not to domestic ones. This distrust is based on: (a) the fact that the 9 problematic cases decided so far are either foreign-to-foreign transactions (the 8 conditional clearances) or projected acquisition by foreign companies of Chinese businesses (1 prohibition decision); (b) the doubts about whether State-owned enterprises and sectoral Chinese companies have to notify and whether compliance with this notification obligation is being effectively supervised and enforced; (c) the possibility for the Chinese competition authorities to consider not only competition concerns but also issues such as the 'development of the national economy' or the 'national (economic) security'. Although the Chinese authorities defend their neutrality and are making some efforts to reduce these concerns, much more transparency and specific action is still needed. This seems to be a crucial issue for the credibility of Chinese merger control.

5. Endnotes

- 1 The Law was adopted on 30 August 2007 and, according to its Article 57, entered into force almost one year later on 1 August 2008. An English translation can be found at the web page of the Chinese Ministry of Foreign Trade (hereinafter MOFCOM), which is the main authority responsible for merger control in China: <http://policy.mofcom.gov.cn/en/claw!fetch.html?id=e07093>, (accessed 31 October 2011).
- 2 Prior to the AML, only foreign acquisitions and concentrations in certain specific sectors were subject to ex ante control.
- 3 MOFCOM Decree no. 6, 2009.
- 4 MOFCOM Decree no. 12, 2009.
- 5 MOFCOM, Notice No. 41, 2010 (Provisional Divestiture Rules). The Provisional Merger Assessment Rules were adopted on 29 August 2011 and took effect on 5 September 2011. In addition, in June 2011 MOFCOM released Draft Interim Measures for Investigating and Disposing of Concentrations of Business Operators Failing to File Notification (hereinafter Draft Rules on Failing to File).
- 6 See Li-fen, W., 2010, pp 477–497.
- 7 Regulation (EC) no. 139/2004 of the Council of 20 January 2004, OJ L 24 of 29 January 2004, p 1.
- 8 Compare with Article 3.2 of Reg. 139/2004: ‘possibility of exercising decisive influence over an undertaking’.
- 9 Interpretative notices were quickly adopted before the entry into force of the first EC merger control regulation in the 90’s. Nowadays, guidelines are contained in the so-called EC jurisdictional consolidated notice, OJ C 95 of 16 April 2008.
- 10 A detailed analysis of this evolution up to the current system can be found in Maillo, J., 2007.
- 11 French, N. and M. Han, 2010, pp 93–94.
- 12 Corr, Ch. and X. Li, 2009, pp 78–79.
- 13 See Article 3 of Decree N° 529 of 1 August 2008. Paragraph 2 of Article 3 announced the adoption of special rules for sectors such as banking, insurance, securities, futures, etc.
- 14 See for example, in the EU case, the short notification form included in Commission Regulation (EC) No. 802/2004, Implementing Regulation of Council Regulation (EC) No. 139/2004, OJ L 133 of 30 April 2004, p. 1–39, as amended by Commission Regulation (EC) No. 1033/2008, OJ 279 of 22 October 2008, p. 3–12. See also Commission Notice on a simplified procedure for treatment of certain concentrations under Council Regulation (EC) no. 139/2004, OJ C 56 of 5 March 2005, p 32–35.
- 15 See Article 2 AML laying down that it ‘shall apply to conducts outside of the territory of the PRC if they eliminate or have restrictive effect on competition on the domestic market of the PRC’.
- 16 Furse, M., 2009, p. 101, at 2–4.07.
- 17 Article 21 AML
- 18 In the EU, Article 7 of Reg. 139/2004 lays down the suspension obligation as a general rule but foresees an exception to the suspension obligation in cases of public bids –Article 7.2 of Reg. 139/2004– and the possibility of applying for a suspension in other cases –Article 7.3 of Reg. 139/2004–.
- 19 Article 48 AML. In the EU, the fine is potentially much higher as the only fine limit is that it cannot exceed 10 % of the turnover of the undertaking(s) concerned. See Article 14.2 of Reg. 139/2004.
- 20 Article 25 AML.
- 21 According to Article 26 AML, the time limit may be extended to no more than 60 days in three cases: first, the parties concerned agree to extend it; second, the documents submitted are inaccurate and/or need further verification; third, the situation has significantly changed since the notification.

- 22 See Article 26 AML and, regarding conditions/remedies, Articles 29 and 30 AML.
- 23 Article 26, last indent, AML.
- 24 It is noteworthy to observe that the only reference to an obligation to state reasons in the AML refers to prohibition decisions: see Article 26 AML.
- 25 Emphasis added.
- 26 In a similar way the ‘substantial lessening of competition’ is the test used in the US.
- 27 OJEC C 31 of 5 February 2004, p 5.
- 28 See EC Regulation 4064/89, OJEC L 395 of 30 December 1989, p 1.
- 29 See Article 27 (6) of the AML explicitly giving to the Chinese authorities the possibility of considering ‘other elements that may have an effect on the market competition’.
- 30 See, for instance, Article 2, 1, b) of the EU Merger Control Regulation (Reg. 139/2004) for a very similar list.
- 31 See below section 2.2., 4)
- 32 See paras. 76–88 of the Commission Guidelines for the assessment of horizontal concentrations
- 33 *Ibid*, para. 85.
- 34 *Ibid*, paras. 89–91.
- 35 See Article 2.2 and 2.3 of Regulation 139/2004 and also section II.2. i) above.
- 36 See Article 2.4 and 2.5 of Regulation 139/2004.
- 37 See Articles 6,1,b) and 8.1–2 of Regulation 139/2004 as well as Commission Notice concerning restrictions directly related and necessary to concentrations, OJ C 56 of 5 March 2005, p 24–31.
- 38 See Article 6.2 and 8.2 of Regulation 139/2004. See also Commission notice on remedies acceptable under Council Regulation (EC) no. 139/2004 and Commission Regulation no. 802/2004, OJ C 267 of 22 October 2008.
- 39 MOFCOM, Decree no. 12 of 2009.
- 40 Article 11 of the Concentration Review Rules 2009.
- 41 Regarding divestitures see the Provisional Divestiture Rules.
- 42 See Article 12 of the Concentration Review Rules.
- 43 See Article 15 of the Concentration Review Rules.
- 44 See Provisional Divestiture Rules.
- 45 For more details on the entry and national security review, see Li-fen, W. 2010, pp 477–497.
- 46 See Huang, Y., 2008, p 128. See also, Furse 2009, 2–4.02; French and Han, 2010, para. 20.
- 47 See inter alia, Furse, 2009; Wang, X.2008, p.2; Di Federico, G.2009,p. 249; Li-fen 2010;
- 48 See article 30 AML.
- 49 All of them will be commented below, in section III.4.
- 50 See Article 20 of Reg. 139/2004.
- 51 All data mentioned in this section are obtained from press conferences/releases and interviews to senior officials of MOFCOM and some law firms’ reports of the enforcement of merger control in China. See in particular, Quinfen, D. 2010, available at http://www.chinadaily.com.cn/bizchina/2010-08/13/content_11148199.htm. (accessed 31 October 2011). See also Deng, F, S. Harris, Jr. and Y. Zhang, 2011, www.antitrustsource.com (accessed 31 October 2011) and *MOFCOM Held Press Conference on the monographic*

Topic of Anti-Monopoly work on August 12, 12 August 2010, cited at Bush, N. and Y. Bo 2011. Regarding Law firms' reports, see inter alia, Mayer Brown, 2 March & 5 March 2010 respectively.

- 52 According to Brown, M., 2010: 'Although it is widely perceived that this step in the approval process is an administrative formality, it has occasionally resulted in delays in approval decisions (when officials have been unavailable for extended periods).'
- 53 MOFCOM, Notice No. 22, 2009 of 18 March 2009.
- 54 InBev/AB, MOFCOM, Notice no. 95, 2008 of 18 November 2008; Mitsubishi/Lucite, MOFCOM Notice no. 28, 2009 of 24 April 2009; GM/Delphi, MOFCOM Notice no. 76, 2009 of 28 September 2009; Pfizer/Wyeth, MOFCOM Notice no. 77, 2009 of 29 September 2009; Panasonic/Sanyo, MOFCOM Notice no. 82, 2009 of 30 October 2009; Novartis/Alcon, MOFCOM Notice no. 53, 2010 of 13 August 2010; Uralkali/Silvinit, MOFCOM Notice of 2 June 2011; Alpha V/Savio, MOFCOM Notice of 31 October 2011. All these decisions are published in Chinese at MOFCOM's web site (<http://fdj.mofcom.gov.cn>). Unofficial translations of these decisions or detailed comments on them are available from the web sites of several international law firms.
- 55 See above section 2.1.
- 56 Interview to the head of MOFCOM's merger control unit on 12 August 2010, cited at Wei, Emch, McGinty and Wheare, MOFCOM Issues conditional clearance of Novartis/Alcon Transaction, <http://www.lexology.com/library/detail.aspx?g=6eb78fe5-407d-4062-908e-d6a72680ef62> (accessed 31 October 2011)
- 57 See Brown, M., 2010, answer to question 5.
- 58 See above section 2.1.
- 59 French and Han, 2010, p 93.
- 60 Corr and Li 2009, p. 78.
- 61 Indeed, the recent decision in case Alpha V/Savio has increased uncertainties. If former decisions seem to suggest that merger control will only be exercised, as in the EU, when a minority shareholding leads to an acquisition of decisive influence (control), Alpha V/Savio treated a shareholding of 27.9% in a competitor as decisive influence although MOFCOM could only reach the conclusion that Alpha's influence 'could not be ruled out'.
- 62 See Brown, M., 2010, answer to question 7.
- 63 With regard to Chinese authorities, see Shan Ming's interview in antitrust source, Deng, E, S. Harris Jr. and Y. Zhang 2011, p. 5...'there are a small number of undertakings whose concentrations exceeded the notification threshold but did not file as required by the law. This is an outright violation of the law'. In contrast, see Freshfields Briefing of 17 June 2011 –MOFCOM issues draft mergers assessment provisions and rules for the investigation of mergers not notified–, p. 5, available from asianewsletter@freshfields.com holding that 'given the size of the Chinese economy and the level of M&A activity in China, one would have expected MOFCOM to have received many more merger filings'.
- 64 See Brown, M., 2010, answer to question 2.
- 65 Shan Ming's interview in Deng, E, S. Harris Jr. and Y. Zhang 2011, p. 5: 'we will discipline and punish such behaviour'. See also Draft Rules on Failing to File.
- 66 See section 2.2. above.
- 67 The first published decision, InBev/AB, was only half a page long. Substantive assessment was limited to a couple of sentences. The latter decisions are already some pages long and, more importantly, give much more information on some of the relevant factors for a good substantive assessment of the case.
- 68 See Emch, A., 2011
- 69 It should be recalled that the Chinese Anti-Monopoly Commission published in July 2009 Guidelines on the Definition of the Relevant Market.

- 70 For severe criticism of MOFCOM's definition in cases InBev/AB and Coca-Cola/Huiyuan, see Zhang, X., V. Yanhua Zang, and H. Chang, 2008. See also Zhang, X. and V. Yanhua Zhang 2010 477–496.
- 71 InBev/AB, the first published decision, lacked an explicit definition of the relevant market.
- 72 See case Panasonic/Sanyo.
- 73 More than 60% in Coca-Cola/Huiyuan, 64% in Mitsubishi/Lucite, 46.4, 61.6 and 77% in case Panasonic/Sanyo, 49.4% in case Pfizer/Wyeth, 55–60% in case Novartis/Alcon, more than 50% in Uralkali/Silvinit and 100% in Alpha V/Savio.
- 74 See Brown, M., 2010, answer to question 6; Emch 2011, p. 135 and Commission Guidelines for the assessment of horizontal concentrations, paras. 89–91..
- 75 See for instance Mitsubishi/Lucite and Pfizer/Wyeth.
- 76 See Pfizer/Wyeth. MOFCOM published for consultation a Draft Guidance on the Review of Unilateral Effects and Co-ordinated effects on Horizontal Concentrations between Undertakings where some other factor were mentioned.
- 77 See Zhang, X. and Y. Zang 2010, p. 490: '...MOFCOM tended to rely on high market shares to presume market power...' See also Zhang, H., 2010 available at <http://ssrn.com/abstract=1569836>, at the conclusions section: '...MOFCOM seems to have tried to establish a *prima facie* case [...] based mainly on markets shares', (accessed 31 October 2011).
- 78 See Interview with Mingh, S. in Deng, F, S. Harris Jr., and Y. Zhang 2011, p 1.
- 79 See Emch, 2011, p 136.
- 80 For a detailed comment on this case, see Zhang, H., 2010.
- 81 See Zhang, X. & Y. Zhang 2010, p 485.
- 82 There was speculation on whether the prohibition had benefited Coca-Cola because the global financial crisis had pushed the stock prices down substantially. See Zhang, X. and Y. Zhang 2010, p 495.
- 83 See Panasonic/Sanyo.
- 84 See Mitsubishi/Lucite, Pfizer/Wyeth and Panasonic/Sanyo.
- 85 See GM/Delphi.
- 86 See Mitsubishi/Lucite.
- 87 See again Mitsubishi/Lucite.
- 88 See case InBev/AB, Novartis/Alcon (intervention in the medicated eye-care products with an overlapping of just 1%) and Alpha V/Savio.
- 89 See Novartis/Alcon (contact lens care products) and GM/Delphi.
- 90 See Ming, S.'s Interview in Deng, F, S. Harris Jr. and Y. Zhang 2011, p 2.
- 91 See section 2.2. 4). above.
- 92 See section 3.4. 2) above.
- 93 See notes 63 and 65 above.
- 94 Circular of the General Office of the State Council on the Establishment of Security Review System regarding Merger and Acquisition of Domestic Enterprises by Foreign Investors, February 3, 2011.
- 95 *Ibid.*, section I (I) and II.

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Conclusions and policy recommendations

As explained by Fernando Delage and Gracia Abad, China's rise is having enormous implications for the international order structure and governance. The book has shown the complex and multidimensional character of the relations between the European Union and China trying to point out the opportunities this cooperation entails.

With the rise of China, India and other emerging nations as major new powers on regional and global level, Europeans have finally realised that a tectonic shift is taking place in the global balance of power, which might have worrying effects in the future. Despite the likelihood of discrepancies and frictions within this relation, the EU and China are meant to play a leading role so that the international community can cope with the new realities.

Although it is claimed that the relation between China and the United States is the most important geopolitical relationship of the 21st century given their economic power and probable strategic competition, the significance of China-EU relations cannot be underestimated. That is probably why the relations between the EU and China have developed so fast over the last few years, as mentioned by Alicia Sorroza and Justo Corti.

As a result, both sides would profit from a closer partnership. Provided that China and the EU can ensure a friendly and productive strategic partnership, they may positively contribute to the surge of a more multilateral world. However, if their relationship becomes frosty, the scenario of competing blocks will become more plausible.

Indeed, China may be considered as one of the leaders in the globalisation process. In joining the international community, it has brought about not only changes but also challenges to the existing order. Its needs and conditions very frequently shape its foreign policy options.

Chinese performance and preferences may raise some concerns for the European Union, as they do not only determine EU influence on economic interests, but also overshadow its role and expectations as a global leading actor. In any case, the Chinese rise constitutes a clear challenge for the EU's economic and social model as well as for the EU's preferred model of global governance.

Accordingly, the viewpoints held by Chinese and European authors in the book reflect not only the differences and disagreements between both actors in some realms but also the areas where fruitful cooperation and collaboration remain possible.

In particular, the importance of multilateralism as a starting point for dialogue and cooperation between the EU and China is a repetitive theme throughout the book. In fact, China's recent interest in multilateralism fits very well with EU's traditional support for multilateralism, even though differences underlying the understanding of the concept cannot be ignored.

In this respect, Weiping Huang and Xinning Song argue that Chinese understanding of multilateralism is very different from the European stance. For the Chinese, multilateralism is a kind of inter-governmental arrangement to deal with common issues. Within the regime, every sovereign state is equal and the main principle is non-intervention in the internal affairs of other nations. For China, multilateralism is better conceived as a kind of diplomatic tool rather than a mechanism of international order. This explains why multilateral diplomacy is a much more popular concept in China than multilateralism itself.

In a similar vein, Maria-Eugenia Bardaro and Frederik Ponjaert compared the European Neighbourhood Policy with Chinese neighbourhood policies. They concluded that, although the PRC China has a specific "Asian Neighbourhood Policy" whose conceptual foundations and methods are similar to the "European Neighbourhood Policy" (ENP), the underlying models are radically different. EU's neighbourhood policy seems a highly efficient functional tool for solving immediate problems. In contrast, China's heterogeneous experiences of multilateralism in its neighbourhood do offer a more strategic outlook towards multilateralism. This has clear implications at domestic, regional and global levels. Bardaro and Ponjaert conclude that whereas the *Neighbourhood Policy* has been a laboratory for EU's multilateral functionalist governance, China's neighbourhoods have been used as testing grounds to display its geo-strategic understanding on multilateralism.

All in all, if cooperation is really to be strengthened in the future, differences between those who understand multilateralism as an instrument of a Westphalian order and those who consider it as a mechanism towards a political system of global governance should be reconciled. In this regard, Mr. Telò advocates to understand New Multilateralism as:

‘[A] form of multilevel collective transnational action and co-operation amongst states and civil societies, regarding global governance and world politics that implies generalized principles of conduct and diffuse reciprocity, and includes several degrees and types of institutionalization, from arrangements and regimes to established organization’¹.

This new multilateral scenario would allow the EU and China to explore potential areas of convergence regarding a rules-based global governance system. Nevertheless, some requirements have to be met for this model to be effective at both regional and international levels:

- A retreat from typically Westphalian frames and concepts such as unipolarism, bipolarism and a multipolar balance of power shall take place. Instead, states shall be considered as political resources for multilateral cooperation.
- The trend towards bilateral and regional fragmentation at different levels shall be reversed;
- Increased synergies between regional and global dimensions of multilevel multilateral cooperation shall be enhanced;
- More efficient and consistent implementation of multilateral commitments shall be ensured through enhanced coordination among multilateral institutions dealing with similar issues and follow-up and monitoring systems;
- Legitimacy, a central challenge for the 21st Century, shall be reinforced. That requires not only efficiency, but also greater transparency and democratic accountability, both at national and supranational levels. In that sense, the civil society, NGOs, networks as well as the private sector must be part of this new era of multilateral, pluralist, multi-actor cooperation.

On the basis of this multilateral approach, J. Lodge and A. Carpenter suggest a range of areas where there is some scope to strengthen the cooperation between the EU and China. In view of the privileged and influential position of the EU and China at regional and global levels, mutual cooperation should be encouraged in order to develop a common frame with global standards in a broad range of activities and policy areas. In this fashion, misconceptions and false assumptions might progressively fade away.

In this sense, the EU and China might develop in a sustained cooperation that might ensure economic stability in the coming years, an issue that is being clearly endangered in the current international context, despite its importance for their trade outlooks.

There are, in particular, two issues where there seems to be room for a potential enhancement of mutual cooperation, at least as they are conceived from an EU standpoint:

Support for socioeconomic reforms, sustainable development, good governance and the rule of law.

The use of multilateralism as a strategy to realise domestic goals. The experience of the EU supranational integration and all its implications in terms of policy-making and regulation might be useful for China. For instance, it would help the People’s Republic to overcome the problem of its highly fragmented internal market. This, in turn, would make it easier to have business and trade relations with third partners, including the European Union itself. Likewise, the regulation of standards for products safety and its implementation policies might constitute areas in which Beijing might learn from the European experience.

Besides, the EU and China should not miss the opportunity to promote greater mutual understanding through formal programmes on cultural and educational exchanges along the initiation of dialogue on social and economic affairs, employment as well as labour policies.

Similarly, Zhimin Chen , Bingran Dai , Zhongqi Pan and Chun Ding hold an optimistic view on the future prospects of the relationship between the EU and China, considering that both parties think strategically and act pragmatically.

Despite Lodge and Carpenter mention that China and the European Union are competitors in the world market for oil, food and raw materials, progress in these realms is best achieved via slow-paced, multilateral diplomacy.

The same applies to those areas of continued tension such as the symbolic 'arms embargo' imposed by the EU members on China which usually have a negative influence on its relationship.

Finally, although it is recognised that the EU-China dialogue is strategically important, it is also claimed that these factors do not automatically give rise to a Strategic Partnership, as many understand. The so called "strategic partnership" is not strategic in the strict sense of the word. Regrettably, despite some consensus between China and EU on several issues, there are still many differences that cannot be underestimated (human rights respect, the arms embargo, the trade imbalance, market economy status, currency levels and intellectual property rights, among others).

In this sense, Zhimin Chen, Bingran Dai, Zhongqi Pan and Chun Ding are aware that it will be difficult to witness dramatic changes in the relationship as the collaboration enters its more complicated stage. The research carried out in this chapter has generated some remarkable policy recommendations in the areas of Chinese foreign policy.

- Firstly, in order to be a responsive member of the international community, China should put more effort into domestic affairs rather than into foreign affairs.
- Secondly, Chinese foreign policy should contribute to China's domestic development. This inward-looking tendency of Chinese foreign policy is most likely the reason why China focuses more on regional affairs than on global ones.
- Thirdly, China needs to assume its leading role as one of the most powerful economies in the world and take the responsibility to lead the debates in the context of the current economic crisis. In this regard, it must be underlined that:

It is one of the top economic powers in the world, with a large GDP in absolute terms;

It has the largest population in the world, but with an increasing need for highly qualified people. The skills of human resources in China should also be improved if modernization is to be achieved;

China shows the patterns of highly developed industrial countries, especially in some areas of high technology. However, the duality underlying social structures - the simultaneous co-existence of rich and poor, advanced and developing regions - should be overcome. Further, the Chinese economy should focus its efforts on building a post-industrialized information society;

Another priority is a more rational allocation of different production resources in order to achieve a higher degree of economic efficiency. This will allow greater technical and institutional progress in a market oriented economy;

The Chinese currency should be convertible either in current account or in capital account of balance of payments;

The Chinese huge market demand allows to absorb a large amount of domestic and foreign economic output and to trigger development;

Effective management of assets is another important issue to consider, specially as regards the flows of technical resources, labor force (qualified labor force), capital funds, information and other natural or non-natural resources;

A stable social system, a patterned and institutionalized social life and a harmonious civil society are likewise relevant requirements;

High living standard in cities, towns, and in the rural areas, with safety food, water, and better environments must be secured;

Finally, interest in global economic affairs and great willingness to participate in world economic and political affairs should be encouraged.

In this sense, Enrique Fanjul also indicates that an open dialogue on the exchange rate of the Chinese currency could contribute to build a more balanced view of this issue. The author claims that China should take into consideration that the exchange rate of the currency is not an entirely domestic issue that can be managed with total autonomy. Not in vain, the exchange rate of one currency is determined in relation to the rest of currencies operating in the global market.

Likewise, he considers that certainty as to the situation of international corporations within the Chinese market should be enhanced. It would be important for China to convey this message, backed up by specific measures, that would reduce the current uncertainties about the business climate in China. Since 2009 the perception by international companies of the trade regulatory framework in China has suffered a sharp deterioration. Some specific incidents have contributed heavily to the idea that foreign firms are no longer as welcome as they used to be. The Chinese authorities should, as Fanjul points out, make clear that China has not entered a period of nationalism and economic protectionism.

Thus, the Chinese authorities would have to explain as clearly as possible the specifics of Chinese trade policies and the business context that foreign companies might expect. Improving the certainty as to the context in which trade can be undertaken is highly desirable, considering that uncertainties have a strong negative influence on business activity.

Likewise, the Chinese authorities should identify the sectors in which they intend to maintain restraints on foreign investment in the medium and long term. Further, it should be specified whether measures favouring domestic technologies or public procurement will be adopted, to cite two of the hottest issues at the present time. European companies could then develop appropriate strategies in relation to the Chinese market.

In this sense, as Jeronimo Maillo pointed out, there are still important uncertainties and concerns regarding the concept of concentration, in particular the extent to which minority acquisitions and joint ventures should be notified. He considered that clearer guidance should be given by Chinese authorities either by publishing individual decisions or, preferably, by adopting general guidelines. Given the fact that the concept of concentration is a jurisdictional issue – being a key factor to know whether prior notification is compulsory – companies must have at their disposal sufficient information in advance.

Likewise, Maillo also stressed that strong empirical evidence reveals that Chinese authorities feel confident enough to forbid certain acquisitions. The prohibition in the Coca-Cola case might be interpreted as a signal in that direction. However, it has to be pointed out that Chinese authorities are more willing to negotiate with the undertakings involved in the case rather than issuing a full prohibition notice. Therefore, this is another area where European authorities and states should continue making efforts to encourage a fluent dialogue.

Furthermore, it is possible to infer from Maillo's work that, in general, horizontal and vertical competition concerns as perceived by Chinese authorities seem to be aligned with best international practices, setting aside the exception of the Coca-Cola case. However, the author considers that detailed guidelines are needed, particularly regarding the very broad scope of the substantive test included in the Chinese Antimonopoly Law (AML). In this context, the recent Provisional Merger Assessment Rules are welcome but more detailed guidance would be helpful. It would be crucial also to have a more developed reasoning within the published decisions.

Maillo also highlighted that remedies and conditions are rather common. Conditional clearances (in eight decisions) are preferred to full prohibitions (in one decision), since remedies and conditions have a very important role to play. Both structural and behavioural remedies have been accepted. Nevertheless, the need and the scope of some of these remedies have been quite controversial.

Finally, he underlined the strong concerns existing about the neutrality of Chinese authorities in the implementation of merger regulations to foreign operations, which seems to be applied in a stricter way than in domestic cases. These suspicions are based on the fact that the nine problematic cases decided up to now are

either foreign-to-foreign transactions or projected acquisitions of Chinese businesses by foreign companies. Another argument supporting this idea is related to the lack of clarity about whether State-owned enterprises and sectoral Chinese companies should notify. Further, there is some uncertainty as to whether compliance with this notification requirements would be effectively supervised and enforced. A last reason for concern regarding equal treatment of domestic and foreign concentrations is the possibility for the Chinese competition authorities to consider not only competition issues but also other economic matters such as the 'development of national economy' or 'national (economic) security' in order to prohibit or allow concentrations. Although the Chinese authorities defend their neutrality and make some efforts to reduce these concerns, much more transparency and consistent action is still needed. Maillou asserts that this seems to be a crucial issue for the credibility of Chinese merger control.

Regarding the strengthening of the Sino- European relationship Zhimin Chen, Bingran Dai, Zhongqi Pan and Chun Ding considered that China needs to take a pragmatic –yet proactive– approach. In view of the current complex nature of China-EU relations, China may not expect any easy step forward in the relationship. At the same time, China shall act proactively and take advantage of the opportunities offered by the favourable international climate, the new EU foreign policy frame and the growing desire of some EU Member States to improve cooperation with China amid European debt crisis.

China should also engage actively in reinforcing the different forms of cooperation available within the European Union, with a special focus on the multilateral level. Apart from strengthening the relations with EU institutions and promoting Chinese expertise on EU affairs, China should also make further efforts to strengthen its relations with Member States.

As Europe is developing a global China policy, China shall also build up its global EU policy. Closer and stronger partnerships with the main players in the current global market would add incentives for the EU to work with China. In that regard, there is still much to do for China in the view of growing disputes between China and some of its neighbours, and between China and the United States in the past two years.

As far as the European approach is concerned, as Alicia Sorroza and Justo Corti suggest, the differences among EU Member States have resulted in the lack of a clear political lead as regards the EU policy toward China. This lack of a uniform drive would need to be overcome if the EU is meant to develop a definite approach towards the People's Republic of China.

Likewise, the EU would also need to revisit its policies, in particular as regards its excessive focus on the creation of an institutionalised framework involving the establishment of a number of meetings, summits, dialogues, cooperation projects, and so on. This institutional framework has certainly enhanced mutual understanding, but the difficulties to reach a partnership and cooperation agreement have showed the limits of this approach and the need to shift its focus in the future.

Similarly, the lack of capacity on the EU side to influence the Chinese domestic or international policy deserves some thought. In this sense, as Sorroza and Corti pointed out, even the incorporation of China in the global economy (including trade and investment flows) could not be considered as a result of EU's influence, but rather as a consequence of China's economic model.

In other words, we could easily conclude that the European Union has been losing leadership vis-à-vis the People's Republic of China, a trend which would need to be reversed, at least from an European perspective.

This is not a minor issue considering that if the EU cannot achieve a coherent policy towards China in the near future, it will not have enough influence to undertake this task later on. Basically, the main obstacle in this relation points to the collision of EU and Chinese interests in third regions. As an example, in Latin America and Africa, China and the European Union compete for markets and resources.

In order to improve the EU policy towards China, two main limitations should be taken into account and, if possible, addressed:

- The lack of coordination between the EU institutions and the main member states in their policies.
- The absence of a clear EU leadership in the conformation of an European policy towards China (EU plus member states).

On the first issue, it is essential for the future of the EU-China relationship that the so-called big three (Germany, France and the United Kingdom) agree to pool their efforts and strongly support the EU's position towards China.

On the second issue, the creation of the European External Service is expected to effectively support a real EU leadership. In this regard, the statement of Ms Ashton declaring the strategic partnerships to be one of her main priorities for 2010 and beyond is illustrative. We have entered a post-Lisbon era, but regrettably it seems that this initiative has lost impulse during the last months. The major question is whether the international scenario will give us the time we need for implementing the Lisbon treaty.

Following this line, Enrique Fanjul insisted that European companies should also discuss economic issues with EU senior officials and their national governments, and design a strategy for negotiating with China, both bilaterally and multilaterally. These topics might then be raised under the High Level Economic Dialogue between China Trade and the EU. They might also be discussed in the course of negotiations for granting China Market Economy Status, a status that China would have great interest in obtaining from the EU.

Besides, there seems to have been a lack of ability in the EU to make a critical assessment of the new geopolitical context created by the financial and economic crisis, in an attempt to turn this experience into a valuable lesson to steer future action in its attitude towards new actors, like China.

With the risk of oversimplifying the complexity of the Chinese foreign policy, there are some elements that have to be carefully considered if the European action towards China is to be meaningful.

Accordingly, at least two elements underpinning the Chinese foreign policy rationale have to be carefully considered by European Foreign Policymakers:

- The first one is the uncompromising defence of the principle of "One China", including the full respect of its territorial integrity and sovereignty.
- The second one is the need on behalf of the Chinese regime to sustain the development process and economic growth, as long as these elements are essential for the sustainability and legitimacy of the Chinese political regime, structured around the Chinese Communist Party (CCP). Consequently, the CCP articulates the priorities of the Chinese foreign policy with a clear purpose to ensure the improvement of the living standards of millions of Chinese citizens. This is, and will remain, at least in the medium term, the driving force behind China's external action.

All in all, the EU must also be aware of the important bargaining tools it might rely on:

- Paramount among them is the market economy status (MES) recognition by European countries. The MES is a political instrument that can be used to put some pressure on the Chinese government in other matters, such as the need to appreciate the renminbi, among others.
- The second one is the EU arms embargo that was imposed on China following the events in Tiananmen Square. The EU arms embargo is perceived by the Chinese authorities as undermining, as they are presumed to hold the same status as Sudan or Zimbabwe dictatorial regimes?. Likewise, on the European side, it is considered as a mechanism for putting pressure on China in relation to human rights and the rule of law, apart from being a very sensitive issue in European relations with other partners such as United States or Japan.

Besides, Enrique Fanjul pointed out that a careful and nuanced approach to trade irritants should be considered. On issues like the exchange rate of the Chinese currency, or the alleged dumping of Chinese products, the situation may be much more complicated than it might seem at first sight. On this sensitive issue, and with regard to the EU action, Fanjul claims that it is important to take into consideration the views of the various economic sectors involved, since some antidumping measures taken by the Commission have been vigorously challenged by certain industries.

The EU, within the context of trade disputes, should as far as possible seek multilateral channels through which conflicts might be better solved. The bargaining power of the EU might be stronger when dealing with a multilateral conflict rather than in the context of a strictly considered bilateral case.

Further, as far as investment is concerned, Clegg and Voss argue that the expertise across the European Union in diverse sectors suggests that the scope for EU FDI into China should be still greater in the future.

In this sense, EU companies and policy makers should bear in mind that empirical research show that investing opportunities in the Chinese economy are still interesting. As Clegg and Voss highlighted, investments in China addressed at the domestic market are already benefiting from the high rates of growth associated with China.

In the same vein, Jeronimo Maillo emphasised the importance of keeping a close cooperation with Chinese authorities in order to enhance technical assistance in competition matters. Similarly, the increasing weight of the Chinese market within the global economy should not be neglected when building up a solid, transparent, legally certain and non-discriminatory merger control regulatory system.

In general, it is very likely that the global challenges we are currently facing will develop into stronger and more solid ties with China (and other international powers). In other words, it seems clear that the EU institutions, together with the Member States, cannot postpone for much longer a reconsideration of their respective policy strategies towards China.

Finally, as Enrique Fanjul pointed out, both China and the European Union should come to the conclusion that certain particular issues should be prioritised. In that sense, it would be appropriate to set up a policy agenda, which would guide the efforts of dialogue and negotiation between the EU and China. Some of the topics that could be given priority are clean energy and climate change; the restrictions in China on foreign investment; the public procurement policy and Chinese funding for projects developed by EU companies; as well as Chinese investments in Europe.

Last but not least, the authors have made some recommendations regarding the research agenda for the future. They stress that more collaborative work between scholars of international relations (IR) and international business (IB) is needed. The relationship between the two disciplines has been rather unclear for many years.

No doubt actual international relations between sovereign states need to be harmonious, in particular if foreign direct investment and trade relations are to prosper. However, once the rules of the game have been set out, it is then entirely up to the business community to implement the commercial agenda. Obviously there are multiple interactions between the areas of international relations and business in the real world, but there are also multiple opportunities to work together for those academics working in IR and business and economics respectively

The business community normally inflicts some pressure on governments, by lobbying for liberalisation. From this lobbying process firms expect to obtain some benefits, not only for themselves, but also for the expansion of trade and investment in general.

Up to date, we have far too little understanding in academic circles of the complexity of this interrelation between dynamics in the business community and dynamics in the field of International Relations. This lack of understanding and explanations is particularly problematic if we take into account that such interrelation contributes to shape the growth of foreign direct investment. With highly contrasting institutional environments between the European Union and China, and the still substantial level of state-centered influence on outward Chinese investment; relations concerning trade policy clearly demand an in-depth analysis through the adoption of a joint and interdisciplinary IR-IB perspective.

Endnotes

- 1 See Chapter 1, p. 38

Author Biography

José María Beneyto

José María Beneyto is Professor of International Public Law, International Relations and International Business Law at the University CEU San Pablo (Madrid). He is *Jean Monnet* Chair in European Law and the Director of the Institute on European Studies, as *Jean Monnet* Centre of Excellence of the European Commission.

He has an extensive experience both as academic and practitioner. He has published relevant scholarly publications and directed national and international research projects in European Studies and International Relations. His most recent publications include a “Treatise on European Law and Policies of the European Union”, “The European Union as a Global Actor”, “Spanish Foreign Policy”.

Xinning Song

Xinning Song is *Jean Monnet* Professor ad personam at Centre for European Studies at Renmin University of China (CESRUC). He is serving as Director of Institute on Comparative Regional Integration Studies at Tsinghua University (Tsinghua-CRIS) in Beijing, and Senior Research Associate of UNU Institute on Comparative Regional Integration Studies (UNU-CRIS) in Bruges, Belgium. He was the Senior Research Fellow at UNU-CRIS from 2007 to 2010, Director of the Centre for European Studies at Renmin University from 1994 to 2007. He acted also as the Vice Chair of International Politics Department and then the Associate Dean of the School of International Studies at Renmin University of China from 1988 until 2005. He is member of the Editorial/Advisory Board of various academic journals including *Review of International Studies*, *Pacific Review*, *Global Society*, *Journal of European Integration*, *International Spectator*, *Chinese Journal of European Studies*, and *Chinese Social Sciences Quarterly*. His research interest include: international relations theory, international political economy, comparative regional integration, European integration, regional integration in the Asia-Pacific, European politics and external relations, Chinese politics and foreign policy.

Chun Ding

Chun Ding, professor of economics, is the director of Center for European Studies, Dutch Study Center, Fudan University, as well as the secretary general of Chinese Society for EU Studies, member of the World Economic Forum’s Global Agenda Council on Europe 2011, Senior Fellow of Center for European Integration Studies, University of Bonn and member of association of German professors with Chinese roots, etc. He is editor of *Chinese Journal of World Economy Outlook* and the chief editor of Annual Report on European Economic Development. Professor Chun Ding is specialized in the fields of world economy, European economic and social integration, European welfare state, European and Chinese social security system, etc.. He has taken charge of over 20 significant national and international research projects, published over 100 articles, theses, and treatises. His monograph, *Comparative Studies on Performances of Major Four Health Care Systems in the World*, has been awarded Second-Class Prize for Eminent Monographs on Philosophy and Social Sciences in Shanghai in 2008.

Mario Telò

Vice-President of the Institute of European Studies, Université Libre de Bruxelles and professor of Political Science, International Relations as a Honorary ‘J.Monnet Chair’. Member of the Royal Academy of Sciences of Belgium. President of the academic council of the international PhD school of GARNET Network of Excellence (Globalization and Regionalism, 40 universities, 2005-10). He served as advisor to the European Commission, the European parliament and the Presidency of EU Council (2000 and 2007).

He is currently Central coordinator of the Erasmus Mundus Doctoral program GEM (Globalization, Europe, Multilateralism) and 2009-2015 GREEN (2011-15) a global network including 16 universities funded by the 7th Framework program. Visiting professor in European, American, Asian Universities among them: Hamburg Univ., N.J., Hitotsubashi Un. and Chuo University, Tokyo, Fudan-Shanghai, LSE-London.

M.Telò published or edited 25 books and more than 100 scientific articles and bookchapters in several languages. Among them: *European Union and New Regionalism* (ed) Ashgate 2007; *Europe: A Civilian Power?*, Palgrave 2005, *International Relations: a European Perspective*, Brussels Univ. 2008 and Ashgate 2009 (forthcoming in Mandarin) and *The EU and Global Governance*, Routledge, 2009.

He takes part on a regular basis into the media discussion on the European construction and global politics.

Juliet Lodge

Juliet Lodge is Co-Director of the Jean Monnet Centre of Excellence, University of Leeds (UK), member of the OHU global internet governance of the internet & society collaboratory, Berlin and Research Associate at the Centre for Cybercrime and Computer Security, University of Newcastle (UK)

She has published extensively on the EU, its policies and institutions. Her current research focuses on soft diplomacy, cross border e-security, biometrics and interoperability, ethical e-governance and home affairs. She has given evidence on these to national parliaments and the European Parliament. She was honoured and elected European Woman of Europe in 1992.

Angela Carpenter

Angela Carpenter is a Visiting Researcher in Governance, Policy and Environment at the School of Earth and Environment, University of Leeds. She obtained her PhD from that University in May 2005 and her main areas of research focus on, but are not limited to, marine environmental policy and governance, marine pollution from ships, and ports policy in the European Union. Dr Carpenter has recently been undertaking work, with colleagues in the *Jean Monnet* European Centre of Excellence at the University of Leeds, on multilateral relations and soft diplomacy between the EU and China, with particular emphasis on issues of energy, environment, climate change and maritime trade. She has also worked as Academic Advisor on a European Commission funded project to develop a new EU Directive on port reception facilities for ship-generated waste and cargo residues, the original version of this Directive being the basis of her PhD research. Her work been cited widely for example by the National Research Council of the US National Academy of Sciences, by the International Union for Conservation of Nature and Natural Resources (IUCN), and by the Marine Environment Protection Committee of the United Nations International Maritime Organization.

Ponjaert Frederik

PhD Candidate at IEE-ULB & KULeuven. His Thesis Subject is 'Opportunities and limits of regionalism applied to the international system'. It is a comparative study of the East-Asian and the European experiences through an analysis of the respective regional roles played by Japan and Germany.

María Eugenia Bardaro

Maria Eugenia Bardaro is a PhD Candidate in Political Science in co-tutorship at the *Université Libre de Bruxelles* and the *Università degli Studi di Napoli l'Orientale*.

Her dissertation, titled 'Norms in International Relations: the case of Japan's engagement towards South-East Asia', maps the patterns and levels of acceptance of these norms to investigate how they affect political decision-making processes.

She has managed a wide range of collaborative projects between the EU and the higher education sector, and currently works in Brussels the EU institutional field.

Her wider research interests encompass how socialisation dynamics affect international policy-making and the role of regional to national identity in influencing both bi- and multilateral relations.

Weiping Huang

Weiping Huang, PhD professor of School of Economics, Renmin University of China since 1993. He was the Chairman of Department of International Economics and Dean of the School of Economics, Renmin University during 1992-2002. Currently he is the Executive Director of Committee on Economics Education and Exchange with the U.S., member of University Council, Academic Committee of Renmin University, and of the China Academic of Social Science. He is also the member of PECC China Committee. He got his Development Economics Master degree in ISVE, Italy in 1987, as the Senior Fulbright Scholar doing research in Stanford University during 1993-1994, and as junction professor of Dickinson College, U.S.A. in 1995, and Federico II, Italy today. He is the outstanding council member of China World Economy Society, International Trade Association, American Economy Studies Association, European Studies Association in China, He is also the consultant for some local authorities and Companies. His research interest includes International Economic Relations, Trade Theories & Policies, and China's Economic Development. His works include 'Toward Globalization', 'Four Tigers in East Asia', 'International Economics', 'The Myth of the World Economy' (all in Chinese), etc.

Bingran Dai

Bingran Dai, born in March 1940, is Jean Monnet Chair *ad personam* (2009) and Honourable Director of the Centre of European Studies, Fudan University. He began his European studies when he joined Fudan University in the 1978, and has since been active in the field both in teaching and research. His further education includes 2 years at LSE (1983 to 1985) as visiting scholar, and 1 year at EUI as *Jean Monnet* Fellow. He was Director of the Fudan Centre between 1998 and 2004, when it became a *Jean Monnet* Centre of Excellence (2004). He is among the first 3 *Jean Monnet* Chairs in China (2001), and was awarded by the European Commission with the *Jean Monnet* Prize 2008. His current academic participations include: Chinese Association for European Studies (Vice Chairman), Chinese Society for EU Studies (Vice Chairman), and Shanghai Institute of European Studies (President).

Zhimin Chen

Zhimin Chen is a *Jean Monnet* Chair professor at School of International Relations and Public Affairs, Fudan University, Shanghai. He is a Member of Advisory Board of The Hague Journal of Diplomacy and a member of the editorial committee of The Pacific Review and Asia Europe Journal. His research interests include international relations theory, diplomacy studies, Chinese foreign policy and EU studies. His major recent publications in Chinese include: *China, the United States and Europe: Cooperation and Competition in a New Trilateral Relation* (2011); *Contemporary Diplomacy* (2008); *Foreign Policy Integration in European Union: An Mission Impossible?* (2003, with Gustaaf Geerarts); *Subnational Governments and Foreign Affairs* (2001). He also co-edited (with David Zweig) *China's Reforms and International Political Economy* (Routledge, 2007).

Zhongqi Pan

Zhongqi Pan is a professor at the School of International Relations and Public Affairs, Fudan University; received Ph.D. in international relations in 1999 from Fudan; seconded by China's Foreign Ministry as a First Secretary at Mission of the People's Republic of China to the European Communities; teach international politics at both undergraduate and graduate levels and in both Chinese and English; give course of International Politics and Theories to MA students in the Chinese Politics and Diplomacy program; research on international relations theory, China and international system, China's foreign policy and strategy, China-US and China-EU relations, etc; author of *World Order: Structure, Mechanisms, and Models* (Shanghai: Shanghai Publishing House, 2004) and many articles both in Chinese and in English at various academic periodicals; editor of *Multilateral Governance and International Order* (Shanghai: Shanghai People's Publishing House, 2006) and *China's International Responsibility and Strategy* (Shanghai: Shanghai People's Publishing House, 2008); was research fellow at the Shanghai Institute for International Studies in 2000-2004, visiting scholar to Lund University (2006), the Fairbank Center at Harvard University (2004), the Henry Stimson Center (2001), and University of Tokyo (1999-2000).

Fernando Delage

Fernando Delage is currently Director General for International Relations at the City Council of Madrid. He has been director of Casa Asia in Madrid (2005-10) and managing editor of *Política Exterior* (1993-2005), the leading Spanish journal of international affairs. He is Bachelor of Laws (Seville University), and Master of Arts in International Relations (Keio University, Tokyo). He teaches regularly on international relations in Asia in University San Pablo-CEU, University Complutense of Madrid, and the Higher Center for National Defence Studies (CESEDEN). He's been lecturer on Asian security at Institute General Gutiérrez Mellado, UNED (Spain's Open University), and guest lecturer at Yokohama National University (Japan). Among his recent publications he is editor of *China in the global security system of the 21st century* (in Spanish), 2009.

Gracia Abad

Gracia Abad holds a PhD in International Relations (Honours), a M. Phil in International Relations and a B.A in Political Science from Universidad Complutense de Madrid. She is Lecturer in International Relations and Political Science at Nebrija University. She has also taught undergraduate, graduate and specialisation courses at Saint Louis University, Complutense University of Madrid and University of Salamanca, among others.

Dr. Abad has been visiting fellow at Royal Holloway, University of London; the European Policy Centre (EPC) in Brussels and the Rajaratnam School of International Studies, (former IDSS), in Singapore and guest lecturer at the Richmond and Syracuse Universities, in London. Abad's main research interests are the international relations of the Asia Pacific, with a special focus in Asia-Europe relations, security, international institutions, multilateralism and Chinese foreign and security policy.

She is author and co-author of more than fifty publications and has given conferences in more that fifteen countries on those issues.

Alicia Sorroza

Alicia Sorroza has a degree in International Relations from the Faculty of Political Science and International Relations of Argentina's Universidad Católica de Córdoba and an MA in International Cooperation from the Universidad Complutense's *Instituto Universitario de Desarrollo y Cooperación*. She is research fellow of the Spanish think-tank *Real Instituto Elcano*.

Justo Corti

Justo Corti is research fellow at the Institute for European Studies and lecturer in European Law at the University CEU San Pablo (Madrid). He has a PhD in International Law and a LLM in European Law, both by the University Complutense of Madrid. He was post-doctoral research fellow at the *Centre National de la Recherche Scientifique* (2008) and visiting scholar at University College London (2007). He is member of the Editorial Board of the journal *Revista de Derecho Comunitario Europeo* and correspondent on Biotech aspects in the *European Journal of Risk Regulation* (Lexxion – Berlin).

Enrique Fanjul

Enrique Fanjul was Economic and Commercial Counsellor of the Spanish Embassy in China (1987-1989). In 1998, he was appointed Economic Consultant of the Tianjin Municipal Government (China). He was Chairman of the Spain-China Business Council (1993-2001). Representative of Spain in the Board of Governors of the Asia Europe Foundation (ASEF) in the period 1997-1998. He is Editorial Advisor of Iberchina (www.iberchina.org), probably the main website in Spanish about China, on the net since 2006. He is member of the Editorial Council of the journals *Política Exterior* and *Economía Exterior*. He is author of three books about China.

Jerónimo Maillo

He is full-time Associate Professor of European Union Law at the Law School (CEU San Pablo University, Madrid) and Head of the Public Law Department. He is Senior Research Fellow at the Institute for European Studies and Coordinator of its Centre for Competition Policy, where he coordinates a Master in International Business Law and a Master in European Union (and its related PhD Program in European Studies).

LLM with honors on EU Law from the College of Europe (Bruges), PhD researcher at the European University Institute (Florence, Italy) and Doctor in law (European Doctorate) at CEU San Pablo University.

His research interest focuses on competition law and on other aspects of economic regulation, both in Europe and in other world areas. He has been appointed as an EU Competition Law and Single European Market expert in several international training and research projects. He has published extensively in the area of Competition Law (author of a monograph and a textbook, editor of 5 other books, and author of more than 20 articles in legal journals and book chapters).



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